

**THE TEXT IS FLY
WITHIN THE BOOK
ONLY**

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BY HENRY HAZLITT



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The Author

LIKE the famous British economist Walter Bagehot, whom he admires, Henry Hazlitt has been a writer in diverse fields — literary criticism, philosophy, politics, economics and finance. He was literary editor of *The New York Sun* from 1925 to 1929, literary editor of *The Nation* from 1930 to 1933, and succeeded H. L. Mencken as editor of *The American Mercury* in 1933. One result of his ten years of book-reviewing was “*The Anatomy of Criticism*,” published in 1933. His deep interest in political questions led to the book, “*A New Constitution Now*,” published in 1942.

But except for the interruption of the years devoted to literary criticism, Henry Hazlitt's dominant interest, since he first became a reporter on *The Wall Street Journal* more than thirty years ago, has been in economics and finance. In 1916 he became a member of the financial staff of the *New York Evening Post*. During our participation in the first World War he was in the air service. On his return to civilian life he wrote the financial letter of the *Mechanics & Metals National Bank*, then one of the ten largest banks of the country but since absorbed by *The Chase National Bank*. He was only 26 when he became financial editor of the *New York Evening Mail*. After the disappearance of the *Mail* through its purchase by Frank A. Munsey he became a member of the editorial staff of *Munsey's New York Herald*, a position which he held until that newspaper in turn was acquired by and merged with *The New York Tribune*.

In 1934 Mr. Hazlitt became a member of the editorial staff of *The New York Times*, and in that capacity he wrote most of its financial and economic editorials. He also later wrote the *Monday financial column*. He remained on the staff of *The Times* for twelve years, and in September 1946, he became the writer of the *Business Tides column* for *Newsweek*. In 1946 he

published "Economics In One Lesson," one of the few serious economic works to become a best seller in recent years. The book has been published also in England, and French and Spanish translations will soon appear.

Mr. Hazlitt has addressed many business and university audiences. Early this year he spent a month in Mexico as a visiting lecturer at the Instituto Technologico, and studied economic conditions in that country. This spring he spent two months in Europe, visiting half a dozen countries—Switzerland, France, Belgium, Holland, Sweden and Great Britain — and writing a series of articles on European conditions which appeared in Newsweek.

WILL DOLLARS SAVE THE WORLD?

THERE is a widespread belief that the United States has a duty to lend or give huge sums to other countries, principally in Europe, if it is to save the world from communism and chaos. This belief is held almost as strongly in the United States, which would make the sacrifices, as it is in the European countries that are expected to benefit from them.

In its most widely held form the conclusion rests on the assumption that the present economic difficulties of Europe are in the main the consequences of the destruction and dislocations of war. It is assumed that there is a definite deficit that America can make up by loans or gifts, that America must supply this if Europe is to recover, that Europe's economic recovery is essential for America's prosperity, and that therefore it is "good business" for America to make these gifts or loans, even if the loans are never repaid. The sacrifices in the present, it is argued, will be more than compensated by gains in the future.

This set of assumptions found expression in the celebrated speech of General George C. Marshall, the American Secretary of State, at Harvard on June 5th:

"The truth of the matter is that Europe's requirements, for the next three or four years, of foreign food and other essential products — principally from America — are so much greater than her present ability to pay that she must have substantial additional help, or face economic, social and political deterioration of a very grave character."

The implication of this statement is that Europe's shortages are being imposed upon her by conditions beyond her control, and that the present import surplus of Europe is solely the result of these shortages and not of other factors. This is also the contention that runs throughout the report of sixteen European nations on the Marshall plan.

It would be ungenerous and short-sighted to minimize the appalling physical destruction and the enormous economic and political problems that the last World War brought upon Europe. We can never forget that in the war against Nazism England stood for a whole year alone. Thousands of her houses and factories were destroyed by blitz. Her peacetime equipment ran down. Her export trade was reduced to less than a third. Most of her foreign investments had to be sold.

Yet when all this has been admitted, we must go on to ask ourselves in all candor whether it is the destruction and dislocations of the war or the governmental policies followed since that war which are primarily responsible for the present European crisis. And whatever we decide regarding the causes of the present crisis, we must also keep in mind that the central question we have now to answer is not what caused it, but what measures and policies are most likely to cure it. Our real problem is not the past, but the future.

Let us begin, therefore, by taking a closer look at the existing situation in Europe.

CHAPTER II

PROBLEM No. 1: GERMANY

IN ANY economic survey of Europe, however brief, it is most profitable to begin with Germany. Germany has become the economic cancer spot of Europe. It has been producing a pitiable fraction of its pre-war industrial output. Steel production in the British and American zones, which reached 17,800,000 tons in 1938, has been cut down in 1947 to a bare 2,800,000. To support their own economies, the Allies have tried to encourage at least the production of coal. But the bi-zone in Western Germany, even according to the optimistic estimates of the sixteen European nations reporting on the Marshall plan, will produce only 133,000,000 tons of coal and lignite in 1947 compared with 206,000,000 in 1938. As the Ruhr, second only to Britain, was the greatest pre-war source of Europe's coal supply, the result of this output shrinkage has been to slow down the whole economy of Europe.

The industrial paralysis deliberately imposed on Germany by Allied policy has forced Great Britain and the United States to pay the Germans "reverse reparations." America has had to pour in foodstuffs to check starvation and disease.

All the countries surrounding Germany — Switzerland, France, Belgium, Holland, Denmark, Sweden — whose economies were closely tied in with hers, have suffered through the German collapse. And not merely because of a coal shortage. Holland, to cite but a single illustration, has suffered both as exporter and importer. Its ports of Rotterdam and Amsterdam, which served not only Holland itself, but the great hinterland of which Germany was the most important part, are largely idle because they no longer serve that hinterland. Dutch vege-

table growers find their principal market cut off. On the side of supply, half the machines in Holland are of German make. But spare parts for them cannot under present conditions be obtained from Germany. The result is that when a single part is broken or worn out a whole machine becomes idle. The absence of a machine may in turn slow down a whole factory.

The first key to the revival of Europe, and to the reduction of the strain on the resources of the United States, is the economic revival of Germany.

It is grimly ironic that many of the same people who now tell us that we must pour our money and goods into Europe because European revival is essential to our own, are the very people who have been the most insistent on the policies that make and keep Germany an economic vacuum. For the great obstacle to German recovery today is not the destruction and dislocations of the war, huge as these were. It is the carving up of Germany and the present policies imposed on her by the Allied occupation forces.

The worst situation is undoubtedly in the Russian zone. Under the Potsdam agreement, the Eastern zone of Germany, which grew the foodstuffs on which the Western zones depended, has been cut off by the iron curtain. From behind that curtain we catch only brief and obscure glimpses of the Russian looting, collectivization and terror which have disorganized production in that area and prevented it from either helping or being helped by the industrial output of the Western sections.

Something will undoubtedly be accomplished by the economic merger of the British and American zones. In both zones, however, the socialist and restrictionist policies imposed have reduced and disorganized production to an appalling extent. Even as recently revised, the "level of industry" plan, which prevents various trades from turning out more than a small percentage of their pre-war output, not only destroys incentives, but imposes an arbitrary and impossible relationship of one industry to another, so that not even the low per-

mitted levels of industry can be attained. As the London *Economist* has put it: "What is planned is actually a series of bottlenecks."

No less demoralizing is the combination of a chaotic currency with legal prices and wages ridiculously below what a free market could bring. Add to this an untold number of economic prohibitions, and the requirement of a special license for almost every economic act, and it is hardly surprising that incentives should be non-existent, that labor and materials should be mis-directed, that nothing should be synchronized with anything else, and that production should be utterly demoralized.

As John Davenport, after a visit to Germany, pointed out in the July 1947 issue of *Fortune*, German currency increased from six billion reichsmarks before the rearmament program to about sixty billion after the war, plus an unknown amount — perhaps ten billion or more — turned out by the Russians with plates dutifully supplied by the United States on Lend-lease. Yet despite this multifold increase in the currency, official German prices and wages have been held about where Hitler stopped them in 1936. As Mr. Davenport comments: "The results are precisely what would be expected — a black market, which is now the real market. . . . The farmer certainly has no incentive to produce more food for sale. Better live as well as he can, better hoard as much as he can, and better avoid money like the plague."

Mr. Davenport presents an illuminating quotation from Dr. Walter Eucken, professor of economics at Freiburg University and heir to the German liberal tradition. Here are some excerpts:

"Germany today is suffering acutely from an overdose of planning. The Nazis laid the basis for German economic planning — for armaments and warfare. To our surprise the Allies left things largely as they were. Prices stayed under official control. . . .

"Barter has developed. Especially on weekends, people

are pouring into the countryside — on foot, on bicycles, by train. They are looking for potatoes—now traded potato by potato—for wheat, rye, fruit and vegetables. And what do they offer? Household goods such as linen and furniture, or shoes and watches, or work—repairing wells, windows, and roofs for the farmer. They are rewarded, often for a whole day's labor, with a few pounds of potatoes, half a pound of grain, a small basket of cherries. What one trader could easily ship by train at little cost, thousands now produce by strenuous and wasteful exertion. . . .

“Here we have a modern industrial country, closely packed with a dense population. This country is now evolving an economic structure as primitive as it may have been at the time of Charlemagne. . . . Meanwhile central planning boards continue to issue their inadequate directives.”

As Wilhelm Röpke writes in the September 6 issue of the British magazine *Time and Tide*: “Nothing would suit the Russians better than a decision by the Western Allies which would perpetuate the present economic paralysis of their zones in Germany. . . . It is not a very enlightened policy to stare anxiously into the enormous shell-hole which still goes under the name of Germany while beyond this hole another gang is experimenting with the same sort of explosives which, a short while ago, blew up Germany and a large part of Europe. . . . [Germany's] role has passed eastwards, and it is only political inertia not to recognize this.”

In brief, in using unintelligent means to prevent Germany from again becoming a menace to the world, we have made it a burden to the world. Fortunately, thoughtful and thorough studies of the German economic problem are at last beginning to appear. Rather than expand further upon that problem here, I refer the reader who is interested to the recent studies by Wilhelm Röpke (“The Solution of the German Problem”), by

Lewis H. Brown ("A Report on Germany"), by Gustav Stolper, Herbert Hoover, and others.

In restoring the productivity of Europe it is only common sense to begin with the sector that is most demoralized and over which we have most control.

CHAPTER III

THE POLICIES OF "RURITANIA"

GERMANY is the outstanding case of a demoralized production imposed by stupid controls from without. We come now to countries which have disorganized and prevented production by unintelligent government interference from within. To keep from making this story too repetitive, by discussing the remarkably similar interventions of each government in turn, it will be more convenient to present a sort of composite photograph of the situation in a single country, which we shall call Ruritania. The situation in Ruritania will be found to apply, with only minor modifications, to most of the countries of Europe. While Belgium and Switzerland, for example, have freer economies than those in this composite picture, other nations are subject to even more extensive dictation.

Ruritania's budget is unbalanced. Heavy sums are being spent on armaments, on subsidies to nationalized industries running a deficit, on food subsidies, and on increasing pensions, family allowances, and other forms of social security — but obviously, the government points out, none of these expenditures can be reduced. Tax rates have been kept up or increased on the higher incomes. A capital levy has been added. Further nationalization and socialization are discussed. Sales taxes on luxuries, with one or two exceptions, have been reduced.

It is surely not the finance minister's fault if these arrangements are not bringing in more revenue. Meanwhile the volume of money in circulation has risen enormously and is still rising. The government, however, is holding down interest rates so that it can borrow cheaper and encourage business borrowing. This policy, however, also increases the inflationary pressure.

In fact, artificially low interest rates cannot be achieved except by increasing the volume of money and bank credit; and the volume of money and credit are increased by maintaining a government deficit. But about this nothing is said by government spokesmen.

Yet though the government is itself creating the inflation, it is alarmed by the unpopular consequences of this inflation. It blames all price rises, not on its own inflationary policies, but on "speculators" and "hoarders," and on the greed and rapacity of producers and sellers. It fixes ceiling prices on everything. This dislocates all profit margins. But as goods are produced in accordance with relative profit margins, there is a huge misdirection and waste of capital and labor. It is necessities that are controlled most. It is their prices that are usually held lowest in relation to production cost. It is necessities which are strictly rationed. The inflationary purchasing power hedged off from necessities expends itself on luxuries which are uncontrolled. Necessities are therefore underproduced. Luxuries are overproduced. While labor is diverted by this process to luxury lines there are universal complaints of "labor shortage."

As inadequate profit margins paralyze production, and as artificial price bargains stimulate consumption, an attempt is made to correct the result by rationing, command priorities, and dictated allocations. The shortages brought about by price control are treated as inescapable and inherent. But as all output is interdependent, production all around is slowed down to that of the item in shortest supply.

On its foreign trade Ruritania imposes controls made necessary by, and in turn necessitating, its internal controls. The country has an inflation and wishes to conceal it. It does this internally by price fixing. But one result of this is that monetary purchasing power is kept in excess of the total value of goods as measured in official prices. This produces the "inflationary gap" — i.e., the amount of money or money incomes with no outlet.

If imports are allowed to come in freely, all this excess money (as Sweden discovered) will be used to buy them. Yet Ruritania wants imports of raw materials and machinery, and wants to buy them as cheaply as possible. It attempts to do this by keeping the official exchange rate of its currency arbitrarily high and by making it a crime to buy or sell its currency below this rate. This makes Ruritania's own goods extremely if not prohibitively expensive in terms of foreign currencies. The high rate for its currency, in short, encourages imports and discourages exports. It is also likely to make the American traveler feel that he is being swindled by the compulsion to convert his dollars at the official exchange rate, and so provokes resentment and discourages tourism.

Ruritania tries to cure all this, not by allowing its paper currency to seek its natural supply-and-demand level, but by refusing to permit any import to come in except by special license. It orders manufacturers to set aside specified goods for export and forbids its own citizens to buy at any price the goods so set aside.

The result of refusing to permit its own citizens to buy "luxury" imports with their own money, however, is to hurt the luxury export trade of all other countries. Yet each European country has its own luxury exports which it is eager to push to get dollars or other exchange to buy necessary imports. France has its wines and brandies, perfumes and laces. Holland has its tulip bulbs and fancy cheeses. Switzerland has its embroideries and resort hotels. Each argues that it is unsound and unrealistic to expect people in these trades to turn to other work. Their capital and long-acquired skills are irrevocably invested in what they are doing. It is often a way of life inherited from their fathers and grandfathers. To force them into other lines would involve huge losses and radically dislocate the whole national structure of production. So each country tries to force other countries to take its luxury exports while refusing to take theirs.

The stalemate is broken by bilateral trade treaties in which each country forces its neighbor to take some of its luxuries along with its necessary products. In return it also agrees to take luxuries along with necessities. These treaties, however, do not merely leave matters where they would have been under freedom of trade. Both necessities and luxuries are exchanged against each other at artificial prices, which do not have to meet world competition. Each country is forced to take, not the goods that its consumers want, and in the proportions that they want them, but the luxuries that its neighbor is most eager to get rid of.

Bilateralism is politically popular because its basic principle, "Buy where you sell," is easier to understand than free multilateralism. It is obviously imitated from Schacht and Hitler, who in turn revived a mercantilist fallacy centuries old. "The sneaking arts of underling tradesmen," wrote Adam Smith in condemning it, "are thus erected into political maxims for the conduct of a great empire; for it is the most underling tradesmen only who make it a rule to employ chiefly their own customers."

Bilateralism is a necessary part of a "planned" — that is to say, a *dictated* — economy. The internal restrictions of a dictated economy would break down at once if it permitted free international trade. Internal and external controls necessitate each other. Bilateralism is ideal for government "planners," because it permits them to say just how much of this or that shall be sold or bought, and to or from just what country. This enables them to keep their hands on all the strings of business, to retain life-and-death control over particular industries, and to throw trade this way or that in accordance with their foreign political policy of the moment. But none of this makes either for domestic prosperity or for peaceful, free or stable world trade.

EFFECTS OF OVERVALUED CURRENCIES

SEVERAL important conclusions emerge from this brief survey. The common assumption, as we have already noted, is that the existing economic difficulties of Europe are in the main the consequence of the destruction and dislocations of war. But the foregoing survey should be enough to show that, on the contrary, the main obstacles to European recovery are the present economic policies followed by the governments of Europe.

When a currency is overvalued (to consider the harmful effects of merely one governmental control) it produces a *chronic* surplus of imports over exports. The overvaluation of a nation's currency makes imports cheaper than they would otherwise be in terms of that currency. This naturally encourages people in that nation to increase their purchases of imports. The overvaluation of the currency tends, on the other hand, to make the prices of that nation's exports high in terms of other currencies. This discourages other countries from buying.

Suppose, for example, that a French brandy sells in Paris for 1,200 francs a bottle. The black-market rate for the franc is about 280 to the dollar as this is being written. Let us assume that in a free market the franc would sell a little higher — say about 240 to the dollar. At such a rate the brandy could be bought for \$5 a bottle in American money. But the official rate for the French franc, which the American importer is now forced to pay, is 119 to the dollar. This means that the brandy must cost him more than \$10 a bottle. The arbitrary exchange rate enforced by the French police raises the price as much as would a 100 per cent American import duty (on top of the duty that we actually impose). And this applies to every French import to this country. Is it surprising, apart from any other factor, that France is exporting so relatively little to us?

In the same way, if we look at the problem from the other side, a typewriter that costs \$100 in the United States would

cost a French buyer, if he had to pay 240 francs for the dollar, 24,000 francs. But as he is able, thanks to exchange control and American loans, to get the dollar for only 119 francs, the typewriter costs him less than 12,000 francs. And this applies to every American import to France. Is it surprising that Frenchmen should want to buy a great deal from us?

Because the overvaluation of the franc makes French goods expensive in terms of dollars, the would-be French exporter may have to reduce his price in terms of francs if he is to meet the competition of other sellers, foreign or American, in the American market. Yet he may see no reason for doing this, because he can realize a larger margin of profit on his domestic sales. And inflation at home, by causing a rise in domestic money incomes, will cause a rising home demand for goods which otherwise would be exported. As if all these discouragements to exports were not enough, the French government does not allow the French exporter to keep the dollars he has made from his export sales or to convert them freely. He must turn 90 per cent of his dollar proceeds over to the government. And he must turn them over at the official rate.

It is hardly surprising, in the face of such regulations, that in most European countries there is a *chronic* excess of imports over exports. It is hardly surprising that these countries now buy more than they sell. This trade deficit does not prove, however, as Secretary Marshall's Harvard speech and the report of the sixteen nations assume, that Europe's "requirements" are this much greater than "her present ability to pay." It was not primarily brought about by the destructions of war. This chronic excess of imports is being brought about, on the contrary, by Europe's own governmental policies. It is being financed today mainly by American governmental loans. It will continue as long as those loans continue, and as long as the internal policies responsible for it continue.

CHAPTER IV

THE MYTH OF A "DOLLAR FAMINE"

THIS brings us to the question of the much discussed "dollar shortage." This phrase has become extremely fashionable in Europe. It has even been accepted at its face value by many Americans.

It is of the first importance, if the world is to apply correct remedies for the present crisis, that it separate the sense from the nonsense in these allegations of a world dollar famine. In one sense, of course, Britain (or France, or Mexico, or the Argentine) is correct in attributing its troubles to a "dollar shortage." In the same sense, an American would be correct in saying that the reason he could not pay his grocery bill or buy himself a new car is that he was suffering from a dollar shortage. But such a description does not explain anything. The real question we must answer, either for the foreign nation or the individual citizen, is what causes the dollar shortage.

Now for Britain or Europe or Latin America to describe its plight as a "dollar shortage" is really a way of implying that the situation is somehow our fault. We are being blamed for not supplying enough dollars. The real trouble, however, is that Britain and Europe and Latin America wish to buy more from the United States than they sell to it. They wish to get from us more than they give. They wish to buy more than they can afford to pay for. They are consuming more than they are producing. The only permanent remedy is for them to increase their production or reduce their consumption. As long as they do neither they can only keep up the one-way trade with us with the proceeds of our loans or gifts. We have in fact been supplying the outside world with \$1,000,000,000 worth of goods

and services every month in excess of what we get in return.

In brief, the trouble at bottom is not a shortage of dollars but a shortage of goods and services to exchange for dollars. To talk of a shortage of dollars in any absolute sense is absurd. In the last two years the United States has contributed to the outside world cash and goods estimated at nearly \$17,000,000,000.¹ The gold and dollars now held by the outside world are estimated to reach the unprecedented total of more than \$20,000,000,000.²

Why, in the face of this, does Europe complain more loudly than ever of a "dollar famine"? Why has the world's trade become so unbalanced? The whole answer would be complex; but the chief responsibility must be placed upon government controls. Most of the governments of the world today, by forcing commodity prices below the levels that supply and demand would bring about, are creating artificial bottlenecks and shortages. When they draw on us for the deficiency, they cause shortages and higher prices even here.

But the gravest case of arbitrary price fixing is the overvaluation that nearly all countries place on their own currencies. They will not accept the verdict of the open market as to what those currencies are really worth. They will not even allow that open market to operate.

Nearly every currency in the world (with a few exceptions like the Swiss franc) is overvalued in terms of the dollar. It is precisely this overvaluation which brings about the so-called dollar scarcity. For it not only encourages other countries to increase their buying from us at the same time as it discourages our buying from them, but it leads to a demand for the dollar as a direct investment because it can be bought at bargain prices. This is the situation which the British encountered when they made the pound for a short time freely convertible into dollars. Nearly everybody who had the right to get dollars asked for

¹ *New York Times*, May 25, 1947.

² *National City Bank Monthly Letter*, July, 1947.

them — not necessarily because he wanted American goods instead of British goods, but because pounds were worth less and dollars more than the official rate of exchange between them.

This situation would long ago have corrected itself if it had been left free to do so. When Europe's imports exceeded its exports, the demand for dollars would have raised the price of dollars in European currencies. This would have made American goods more expensive for European buyers at the same time as it made European goods cheaper for Americans. The balance of trade would have been automatically restored.

Moreover, if importers and exporters were free to buy and sell exchange at the rates that supply and demand warranted, all currencies would be freely convertible at a price. In the black market all currencies are in fact convertible at a price. Britain, for example, could convert its "soft" into "hard" currencies at will at prevailing market rates. It is only because people are not allowed to pay or ask the real market rates that the conversion does not take place.

Why is this simple solution to the dollar and foreign-trade problem not adopted? Because under the Bretton Woods agreements (Article IV, Sections 3 and 4) each member of the International Monetary Fund is not merely permitted but *compelled* to forbid currency transactions within its own borders at other than the official rates. There can be no solution of the world unbalance of trade and of the so-called "world dollar famine" until this provision is revised to permit the restoration of free world markets in foreign exchange. Not until such free world markets exist can we tell what the real "needs" of Europe are. We might find, indeed, that the restoration of free markets in exchange, especially if combined with the restoration of free markets in commodities, would make virtually the whole "Marshall plan" unnecessary.

It is important to keep in mind that the "dollar shortage" is not a complaint merely of European nations that have been

ravaged by the war. It is an almost world-wide complaint. It is raised in Canada, Australia, Sweden, Mexico, the Argentine. It exists, in fact, in every country whose currency unit is over-valued compared with the dollar, and where people are not free to deal in that currency unit at its real value.

It is often argued that Britain or France or some other country cannot afford to let its currency fall to the value that a free market would put on it, because this would bring it fewer dollars for the same volume of exports. This argument, however, is based on the tacit assumption that the exported goods — from Britain, say — enjoy a monopoly in the United States, so that Americans are forced to buy them at no matter what price in dollars. There are not many British goods to which this applies — not many which do not face a competitive market here and may not already have priced themselves out of this market. Even where a monopoly situation exists, moreover, the greater number of dollars secured by the pegged sterling rate can easily be more than offset by a more than proportionate shrinkage in the volume of British export sales.

Sometimes the matter is argued from the other end. It is said that England or France cannot afford to let their currencies decline to the free market price because American goods would cost them more in pounds and in francs. It is forgotten that these higher prices might discourage excessive imports from the United States. Even more important, it is forgotten that this whole system of a chronically unbalanced trade can be kept going only by fresh loans from America. Only the continuance of American loans, in brief, has continued to make an over-valued pound or franc possible.

Under a gold standard, when a currency rose or fell beyond a very narrow range in relation to other currencies, shipments of gold corrected the disequilibrium in trade and restored a balance between the supply of and demand for the currency. Sometimes this happened through a rather complicated chain of causation. If a country had an excess of imports because its

prices were too high in relation to world prices, it lost gold (because the value of its currency unit in the foreign exchange market fell to a point where it paid to demand gold in exchange for it). As it lost gold, the contraction in the reserve bases for its money and credit caused a rise in interest rates in that country. This rise in interest rates discouraged borrowing, induced some paying off of existing loans, and so reduced the outstanding volume of money and credit. This contraction of money and credit lowered prices in that country and so brought it into line with world prices and restored or reversed the balance of imports and exports.

Without the gold standard and the free movement of goods this correction in the trade balance can only be made by wide fluctuations in the prices of paper currencies. Where fixed exchange rates make this correction impossible, it is impossible in turn to correct the trade disequilibrium. The countries that refuse to correct their price levels or exchange rates thereupon attribute their troubles to a "shortage of dollars."

When nations are on a gold standard a fixed rate of exchange is both possible and desirable. When each currency is anchored to gold, all currencies are necessarily anchored to each other. Each currency unit can then be expressed as a precise ratio of another. It can be freely and safely converted into it. But when each country is on its own paper standard its currency can have no fixed value in relation to other currencies. It can be given the appearance of such a fixed value only by making it a crime to buy or sell it at any other rate. But this attempt to maintain by coercion the appearance of stability where no stability exists merely makes the economic consequences incomparably worse. And this crucial and central factor in the whole world economic crisis is treated in most discussions of that crisis as if it simply did not exist.

CHAPTER V

PRINCIPLES OF FOREIGN AID

THIS brings us to the basic facts and principles that must be kept in mind in connection with the whole problem of foreign aid:

1. *As the United States produces only 12 per cent of the world's food supply, it is clear that America cannot feed the whole world.*

Before the war, the United States produced less than 9 per cent of the world's food supply as measured in calories. Today, as a result of increase in our own production and the falling off of Europe's, we produce nearly 12 per cent of the total.¹ Even this is hopelessly inadequate to fill the gap left by the decline in European production. America has 140,000,000 mouths to feed; but Europe has 350,000,000. It should be obvious that the real solution is not to distribute scarcity, but to restore production. As we have already seen, this is prevented everywhere in Europe today—by Russian looting, by the policies of the Allied occupation authorities in Germany, by socialism and communism, by “agrarian reforms” which seize land, break up farms and displace populations, by export and import barriers, by exchange controls, and by price-fixing which makes it unprofitable or impossible to grow, transport and sell food. Because of the small American food supply in relation to world demand, the effort to atone even moderately for the food shortages in Europe must cause soaring food prices here.

¹ Before the war, the world produced between 1.8 and 2 million billion food calories, of which the United States produced about 160 thousand billion, or a little over 8½ per cent of the world's food supply. Europe, excluding Russia, produced roughly 350 thousand billion calories—about 18 per cent of the world's supply, or more than twice as much as the United States. In the pre-war period Europe imported from 15 to 20 per cent of its total food supply.

2. *The need for outside help to restore Europe's capital structure has been greatly exaggerated. Its unused resources for creating its own capital are very great.*

As L. Albert Hahn has pointed out in an article called "Capital is Made at Home" (*Social Research*, May, 1944), foreign capital did not flow into Germany in substantial amounts immediately after the First World War, when capital was urgently needed to replace depleted stocks and restore the wornout industrial and transportation systems. Nevertheless, in 1924, after the great inflation, Germany's industrial and transportation systems were in good shape; for meanwhile, except during the dizzy last months of inflation, the German entrepreneur had had more capital at his disposal than he actually needed. "Capital was made at home, through the restrictions that inflation had imposed on consumption."

In 1924, it is true, Germany began to absorb higher amounts of foreign capital, but by mid-July, 1931, the import of capital was suddenly stopped and she was forced to rely on her own resources. "In one week she gave up her search for foreign credits and turned to capital autarky. Nevertheless, as the world has meanwhile come to know to its sorrow, her industrial output was stupendous."

As Dr. Hahn has insisted: "It should never be forgotten that despite the widely held opinion, no country is predestined to have an active or passive trade balance. A small deflationary pressure on the price level, or a small inflationary rise in the price level, will, under certain conditions, suffice to reverse the trend of the trade balance. . . . The Germany that was then professing not to have sufficient foreign exchange for her creditors had all the foreign exchange she needed for her war preparations. Incredible as it seems today, it is clear that a substantial part of Germany's war preparations was financed by her foreign creditors, very much against their will."

3. This brings us to a third principle, which is that *help from outside to any country goes eventually to relieve the*

LEAST urgent needs which the government of that country then decides to meet.

This follows from the ability to divert resources, and from the fact that any country meets first what it considers its most urgent needs—or rather what those in power in that country consider its most urgent needs. Those who tell us, for example, that if we do not send food to the Yugoslavian government we are starving its people, forget that Yugoslavia conscripts an enormous standing army from men who would otherwise work on farms to produce food. To the extent that Yugoslavia's food problem is solved by outside gifts, it releases the manpower and financial resources to maintain this military establishment.

When we keep this elementary principle in mind, we recognize how unimportant and even how futile it is to require that our loans to foreign governments be used only for certain specific purposes. We could, for example, insist that our funds should be used only to buy foodstuffs. But to the extent that we relieve the borrowing country of the need of supplying its own foodstuffs, we merely release resources in that country to supply some less urgent need. Hence it is pointless to insist that the proceeds of our loans should go only for some specified purpose. To the extent that we relieve a foreign government of the need of providing for this purpose, it can use the released resources to increase social security payments, to raise salaries of civil servants, to expand its military establishment, to finance anti-capitalist propaganda, or for any other purpose that it thinks desirable.

This principle is recognized quickly enough when dealing with individuals. If you make a loan to a family that keeps a car for pleasure, nothing is gained by the assurance that the particular dollars you have loaned have gone only to buy food, and that the automobile was bought and run with the family's own earnings. Even if you could verify by the numbers on the bills that your particular dollars were spent only for food, you would know that your loan was being used *in effect* to keep the

car—because the family would otherwise have to give up the car and use its own earnings for the food.

Yet this elementary principle is constantly overlooked in international relations. People feel somehow assured by the statement that our loans or gifts have been earmarked only for special purposes. Unless we undertake to control *all* the expenditures of the borrowing country, however, our particular contribution becomes in practice an unidentifiable part of the general pool out of which that country's expenditures are made, like the last bucketful of water after it has been poured into an already partly-filled tub.

AMERICAN AID VS. EUROPEAN POLICY

4. *Food relief and financial help from the United States will be futile unless the country aided discontinues policies which unbalance its trade and discourage or prevent production.*

Here again everyone recognizes a similar principle in his private affairs. A banker cannot lend the funds which others have entrusted to him to a manufacturer who is so incompetent that he is bound to fail, or who indulges in practices which make it impossible for him to repay the loan. A manufacturer who is following practices which make it impossible for him to maintain his solvency, a manufacturer whose costs exceed his receipts, is simply dissipating resources. To say that his costs are greater than his income is merely another way of saying that the value of the raw materials and labor services he is using up is greater than the value of the finished goods he is producing.

An indulgent father who is lavishing money on a son who merely squanders it in idleness and vice is not doing that son a service. Outside help, whether of loans or gifts, is in general only good to the extent that it promotes self-help.

These principles apply to nations as to individuals. Loans or gifts that merely subsidize or prolong policies that paralyze production are worse than thrown away. Yet we have the

strange spectacle today of Europeans who tell us in effect: "It is your duty to come to our aid; it is your duty to pour your money into our countries; but you must have nothing whatever to say about its use. That would be interfering in our internal affairs; that would be undermining our independence."

Such a position is on its face self-contradictory. A nation that asks for help not based on purely commercial considerations admits that it is dependent. It is asking us to interfere in its affairs, but to interfere solely on its own terms and not on ours. It may be asking us, in effect, to give it funds to maintain, subsidize and prolong the very policies which have brought it to or kept it in its present state.

I should like to present here an instructive quotation:

"The United States is disinclined to entangle herself further (after recent experiences) in the affairs of Europe, and, anyhow, has for the time being no more capital to spare for export on a large scale. There is no guarantee that Europe will put financial assistance to proper use, or that she will not squander it and be in just as bad case two or three years hence as she is now. . . . In short, America would have postponed her own capital development and raised her own cost of living in order that Europe might continue for another year or two the practices, the policy, and the men of the past nine months. . . .

"If I had influence at the United States Treasury, I would not lend a penny to a single one of the present Governments of Europe. They are not to be trusted with resources which they would devote to the furtherance of policies in repugnance to which, in spite of the President's failure to assert either the might or the ideals of the people of the United States, the Republican and the Democratic parties are probably united."

These are not the words of some American "isolationist" in 1947. They are the words of the most influential British economist of the last generation. They were written in 1919 by John

Maynard Keynes in "The Economic Consequences of the Peace" (pp. 283-5). They apply with startling accuracy to conditions today.

It is true that in 1919 Mr. Keynes did favor an American loan to Europe—of the very modest amount, by present standards, of \$1,000,000,000 in the first instance—but only on the assumption that Europe would agree to these very drastic conditions:

"This sum . . . should be lent and should be borrowed with the unequivocal intention of its being repaid in full. With this object in view, the security for the loan should be the best obtainable, and the arrangements for its ultimate repayment as complete as possible. In particular, it should rank, both for payment of interest and discharge of capital, in front of all Reparation claims, all inter-Ally War Debt, all internal war loans, and all other Government indebtedness of any other kind. Those borrowing countries who will be entitled to Reparation payments should be required to pledge all such receipts to repayment of the new loan. And all the borrowing countries should be required to place their customs duties on a gold basis and to pledge such receipts to its service.

"Expenditure out of the loan should be subject to general, but not detailed, supervision by the lending countries."

THE MINIMUM REFORMS NEEDED

IF WE grant, then, that any financial aid we extended to Europe would be futile unless accompanied by drastic economic reforms in the recipient countries, what are the *minimum* reforms that would be needed to bring recovery? They would include the following:

I. A balanced budget. Unless a government's revenues equal or exceed its expenditures it cannot prevent inflation; it cannot stabilize its currency. The greater part of the network of

controls that are strangling European production and European liberty today began as an effort to prevent the consequences of a currency inflation. Nearly all governments, of course, will argue that they are too poor to balance their budgets; that their revenues are insufficient. The answer will be found in pointing to their expenditures, which are in most cases enormously greater than before the war. This is the result of larger military establishments, bigger social security schemes, food subsidies, bigger subsidies to meet bigger deficits in nationalized industries, grandiose government building schemes, industrialization programs, and what-not. If they are "too poor" to balance their budget, they may appropriately be asked, are they rich enough to afford these?

II. The elimination of exchange controls. There will be no long-term economic stability and no real freedom of international trade until nations go back to the gold standard. But the first step toward the resumption of free and normal international trade is the removal of all prohibitions on the rate at which the existing paper currency is bought and sold, either in terms of gold or of other currencies.

This does not mean immediate "devaluation." "Devaluation" is, in fact, meaningless except in relation to a gold standard — or at least to something definite into which the currency is freely convertible. Otherwise we should have to ask, "Devaluation" in terms of what? "Devaluation" in relation to what? As long as a currency is not convertible, it is useless for the government authorities to put any arbitrary "official" value on it (in terms of American dollars, say). They can only make this partially (and dangerously) effective by making it a crime for anybody to buy or sell the currency below that value.

A borrowing government may therefore at least temporarily retain its existing "official" currency rate if it thinks that rate has still any purpose or significance. For its real depreciation has already taken place; it is merely a question of the government's being willing to acknowledge the existence of that de-

preciation. Only if the currency rate is left free — until a self-stabilizing gold standard can be re-established — can there be a resumption of a healthy, normal, two-way foreign trade.

III. There must be an end of price control, either for home-produced or imported goods, and an end of other regulations that prevent or unbalance trade and production.

IV. Excessive foreign trade barriers must be lowered or removed.

V. As American loans or gifts would in effect be used to support the recipient country's military establishment (either directly or by releasing the resources devoted to it), an excessive military establishment could not be permitted.

The American government has in fact imposed some conditions with many of the loans and gifts it has made. In most cases these conditions have been wholly inadequate. In others they have been worse than nothing. Instead of asking for fewer governmental controls, our government has asked for more.

In reply to its request, it got "assurances" from Greece, for example, that: "Existing regulations on the import and export of foreign exchange will be enforced and strengthened by all possible means. . . . A vigorous program will be undertaken to hold down prices and to establish an equitable relationship between prices and wages. . . . Rent control and rationing of commodities will be continued. . . . The Greek Government would also wish the [American] mission to assist in . . . regulation of wages and prices."¹

The American officials who insisted on these conditions did not know that exchange control, price control and wage control are not the way to check inflation; they are merely the way to check production.

¹Greek Government's reply of June 15, 1947 to American Note.
New York Times, June 19, 1947.

THE DILEMMA OF CONDITIONS

MANY Americans recognize that financial aid to Europe will be futile unless European governments change their present economic policies. But most people assume that this difficulty can be met if our government attaches conditions to its aid similar to those just outlined. This view, however, faces grave dilemmas both at the borrowing and at the lending end.

The borrowing governments believe in the economic policies they are following. They think these policies essential to revival, or at worst "unavoidable." For at least three main reasons they resent any conditions imposed on them.

1. They will insist that these conditions are impossible of fulfillment, or that they will actually prevent revival, or even that they will bring "economic chaos." Anything that goes wrong will be blamed not on their other policies but merely on whatever they have done to conform with the conditions of the loan.

2. Any conditions whatever, from the mere fact that they *are* conditions, will be considered humiliating. The borrowing government will regard them as an infringement of its sovereignty and independence. It will be accused of subservience and vassalage by the Communists and by its domestic opposition. America will be accused of using the loan to seek political domination.

3. The borrowing nation is certain to suspect that any conditions imposed by the lender are primarily for the lender's benefit and not for its own. Thus, though the main purpose of the American government is the economic revival of Europe, and though the conditions it imposes are solely designed to make sure that its loans or gifts will bring this revival, the very fact that the American government insists on those conditions will be enough to make them unpopular in the borrowing countries. European governments will think of themselves as

making these reforms, not for the recovery of their own country, but *as a favor to us*. Even if they do recover, they are almost certain to conclude that they recovered in spite of the reforms and not because of them. And if conditions in the borrowing country actually become worse —

But we can get a sufficient foretaste of the future from the past, and we need merely quote what the supposedly conservative and responsible London *Economist* had to say in its issue of August 23, 1947 about the conditions of the American loan:

“American opinion should be warned that over here, in Great Britain, one has the feeling of being driven into a corner by a complex of American actions and insistencies which, in combination, are quite intolerable. Not many people in this country believe the Communist thesis that it is the deliberate and conscious aim of American policy to ruin Britain and everything that Britain stands for in the world. But the evidence can certainly be read that way. And if every time that aid is extended conditions are attached which make it impossible for Britain ever to escape the necessity of going back for still more aid, obtained with still more self-abasement and on still more crippling terms, then the result will certainly be what the Communists predict, whether or not it is what the Americans intend. The crippling of the British export trades that was one of the conditions of Lend-lease increased the dimensions of the aid that was required in 1945. And the famous Articles Seven to Ten of the Loan Agreement, with their obligations of convertibility and non-discrimination, have brought the British back to Washington earlier and in worse plight than was necessary. . . .

“The risks of convertibility have proved all too real. Non-discrimination, if it is applied in the months to come, will be the means of starving the British people. Yet even now at Geneva the British representatives are in process of committing this country, in the proposed Charter of the

International Trade Organization, to sweeping general principles which, however excellent they may be in theory, are likely to prove in practice to be equally dangerous. . . .

“For the present, the Americans still retain the power to make the British Government jump through any hoop they choose. . . . Let them forget, for the moment, their own conviction that their present wealth and strength are the result of superior virtue and remember the Europeans’ conviction that they are merely due to better luck.”

So much for the dilemmas that the effort to impose even the mildest common-sense conditions is likely to meet from the borrowing end.

But we face today a scarcely less serious dilemma from the lending end. The only conditions that could really bring revival to a borrowing country are those that stabilize the real value of its currency (as opposed to the “official” value) and that restore free markets. But these are not the conditions in which most of our own government representatives abroad really believe. As illustrated by the policies they have approved for or imposed on Greece, Germany and Japan, they believe fundamentally in Schachtism — i.e., in price control, wage control, trade control, exchange control and in government production “targets.” Many of them are either convinced outright that nationalization is better than private enterprise or at worse consider it a matter of indifference or of purely academic importance which system a nation adopts.

There is no assurance, if our government officials impose conditions with their loans, that they will not impose precisely the conditions that hinder recovery and lead toward a totalitarian economy.

POLICIES MORE IMPORTANT THAN LOANS

5. *As a contribution to revival, the economic policies followed by a country are much more important than any foreign loan.*

This should be evident from a simple mathematical calculation. By far the greatest post-war loan so far made by the United States to any foreign country is that of \$3,750,000,000 to Great Britain. Britain used up \$2,450,000,000 of this loan in the first twelve months. The national income of Great Britain in 1946, as estimated in a Government White Paper,¹ was £7,974,000,000, or approximately (at \$4 to the pound) \$31,896,000,000. The dollar credit, then, was being used at a rate which, high as it is, is still less than 8 per cent of the British national income. A 10 per cent increase in Britain's production, therefore, particularly if reflected in a changed relation of imports and exports, would do far more for Britain than the American dollar loan. Even without such an increased production a change in Britain's currency control policies could restore the trade balance.

The situation of England in this respect is not different from that of other European countries. A removal of the present throttling controls would easily permit at least a 10 per cent over-all improvement in production. Yet an over-all amount equal to 10 per cent of Europe's present national income is more than the United States could possibly contribute in loans or gifts.

If it were possible successfully to impose sound policies as a condition for our loans, the conditions would be more important than the loans themselves.

¹ National Income and Expenditure of the United Kingdom, 1938 to 1946. April, 1947.

SETTING AN EXAMPLE

6. *The United States government cannot consistently recommend sound policies to foreign governments as a condition for loans, when it is not following such policies itself. It can preach effectively only by example. And it can do more for world revival by making its own economy sound and strong and free than by trying to put temporary props under economies built on the treacherous foundations of totalitarian controls.*

The United States today has what is still called a "free" economy. It deserves this title only by contrast with a regimented world. It would not have been called a free economy twenty years ago. It will not function with the resilience of a genuinely free economy. We must reduce our unparalleled Federal expenses, still running at a rate five times as great as immediately before the war. We must reduce taxes to a level under which a healthy private enterprise can permanently function. We must cease trying to maintain absurdly low interest rates by inflationary means. We must return to a real instead of a merely technical gold standard.

And one major responsibility of the American government is to lower its tariffs. We cannot restore the balance of trade unless we are willing to buy as well as sell. We must remove every unreasonable barrier to the entrance of foreign goods. Our loans can be repaid only if we are willing to accept repayment. The only ultimate way in which we can accept repayment is in goods and services.

This also conforms to the principle that the best kind of help is the kind that promotes self-help. The best help to an unemployed man is not a loan or a gift, but a job. This maintains his self-respect and independence; it enables him to contribute services of a value at least equal to what he receives; it adds to the national income. For like reasons, the best way

to help Europe is not to make doubtful loans or gifts, but to buy her goods.

When all this is said, however, it should be added that in recent years the tariff issue, and particularly the American tariff issue, has been greatly exaggerated as compared with its real importance. The world has now adopted barriers which are enormously more serious obstacles to trade than even high tariff walls. These include bilateralism, exchange control, quotas, special licenses, and direct prohibitions of imports and exports. The American tariff is today a minor rather than a major reason for the unbalance in American trade. Our imports are today held down more by the practices of foreign governments than by our own. And it is far from certain that the American tariff is today as high compared with other tariffs as most Europeans like to believe.¹

All this does not mean that the United States should not reduce its tariffs further, *whether other nations do so or not*. The fact that there are today much more serious barriers to trade than tariffs does not mean that we should not do everything we reasonably can to reduce our own tariffs. At a time, indeed, when foreign nations have drastically reduced their own potential exports by their overvalued currencies, we have a unique opportunity to make sharp cuts in our import duties with a minimum of disturbance.

¹A more thorough study of this subject is needed than any that has yet been made. The construction of comparative tariff indices would be subject to many pitfalls and dangers of interpretation. But tariff comparisons through a carefully considered set of indices would certainly be better than leaving the question to mere rhetoric or vague impression.

LOANS PROLONG CONTROLS

7. *Inter-governmental loans increase and prolong governmental restrictions on the economy both in the borrowing and in the lending country.*

They do this in the first place because they subsidize restrictions on the part of the borrowing country. But they do it also because, when the government makes itself responsible for bringing in more foreign exchange by borrowing, it also assumes responsibility for the way in which that foreign exchange is allocated. Hence import ceilings, import quotas and import licenses become an inherent part of the government borrowing program.

But the lending country is no less affected, though in a different way. When the American government makes loans to a foreign government, it transfers purchasing power from the hands of its own citizens to that of the foreign government. In addition, unless the loans are immediately offset by the same amount of additional taxes, it creates inflationary purchasing power bidding for the limited supply of its domestic goods. It then, in order to make sure of keeping in the country goods needed by its own consumers or raw materials needed by its own manufacturers, insists that it continue to have the wartime power to impose export quotas. Export controls by our Federal Government have been kept for precisely this reason.

Inter-governmental loans prolong government controls and delay the return to a free economy.

WHO SUBSIDIZES WHOM?

8. *The bulk of our past and prospective government "loans" to foreign governments are little better than thinly disguised gifts.*

It would hardly be realistic, certainly, to adopt any other assumption in view of the history of inter-governmental loans,

and particularly of the loans we made in expectation of repayment in the First World War. Conditions then were in fact not nearly as chaotic as today. At that time some of the borrowing governments had been accustomed to respect their agreements. They had not yet built up the precedents and self-justifications for default and repudiation that they have now.

But if we adopt this realistic view, it must have important effects upon our present policy and upon our expectations concerning its consequences. It merely breeds ill-feeling on both sides if something that was originally treated as a loan is defaulted.

Moreover, if our present "loans" are really gifts, we are deceiving ourselves if we put them down as assets. The money handed out is a direct loss. It must soon or late be repaid in our tax bills. This means, for one thing, that the "loans" our government makes to foreign governments must be treated like any other government expenditure. If they are not to be inflationary, unbalancing the budget, they must be met out of immediate increased taxes. When we are discussing how much foreign aid we can "afford," we must discuss how much additional taxation we can afford.

We cannot adopt the realistic view that these so-called loans are really disguised gifts, without raising the further question concerning who is subsidizing whom. The most frequently urged reason for loans or gifts from the United States to Europe is that "Europe" is "poor" and the "United States" is "rich." But this simple statement conceals a very complicated set of facts. It means that the *average* income of *families and individuals* in the United States is higher than the *average* income of *families and individuals* in Europe. And that is all it does mean. There are many people in Europe richer than the average American. These wealthy Europeans will necessarily be beneficiaries, directly or indirectly, of loans and gifts from the United States. All Americans, poor as well as rich, will necessarily be the losers, directly or indirectly, from these loans or

gifts—whether by higher taxes, higher food prices, goods shortages, or in other ways.

Probably the chief source of pressure for loans and gifts from “America” to “Europe” arises out of a confused egalitarian philosophy which assumes that it is a duty of the “richer” nations to share their wealth with the “poorer.” The consistent application of such a philosophy would, of course, also make it incumbent upon “Europe” to share its wealth with “India” and “China” and “Africa.” Consistency would, in fact, first of all require the equalization of incomes both within the United States and within Europe. But without going into the implications of economic egalitarianism, it is sufficient for present purposes to point out that under the program of gift-loans from “America” to “Europe” lower-income persons and groups in America are in effect subsidizing some persons and groups in Europe with incomes higher than themselves.

CHAPTER VI

WILL FOREIGN LOANS MAKE US RICH?

9. *It is not true that the United States needs foreign loans to keep full production and employment at home. It is not true that we can get rich by giving our goods away.*

More and more the strange idea is being put forward that America must make loans or gifts to foreign countries, not primarily to save them, but to save itself. We are told that our government must make these gifts or loans not as a humane or charitable duty but out of shrewd self-interest. Newspaper commentators in the recipient countries have more and more been interpreting our government's generosity to them on this theory. As early as June 25, 1947, *Pravda* declared that the Marshall plan was influenced by a desire to prolong a post-war "boom in the United States" and to "lessen the ripening economic crisis" here.

That Communist Russia should hold such a view is not surprising. It fits in perfectly with all the other claptrap that Communists have long preached about capitalism. But the theory is just as eagerly embraced elsewhere.

In its issue of July 12, 1946, the *Eastern Economist* of New Delhi put it forward in its most naked form:

"The U. S. Lend-lease plan of helping the Allies in the recent war has been acclaimed as an act of unparalleled generosity," (it said). "But it was also a brilliant and ingenious way of solving what would otherwise have been an intractable problem. . . . The productive power of America has multiplied itself so fast that it is now admitted that she cannot continue to give 60 million jobs unless she is able to have a large export trade. . . . In such circum-

stances it would not be such a foolish thing (as some might imagine) to give away goods to other countries, for on balance it would be better to part with surplus goods than to create unemployment. . . . Machinery would be set up by America whose purpose would be to provide *gifts* of loans to countries. . . . The U. S. Government will buy the goods, give them as gifts and reimburse itself by additional internal taxation. . . . If this is to play the world's Santa Claus, the United States of America is both rich enough and should have sense enough to fill the role."

This idea, in both crude and sophisticated guise, has been endlessly repeated in the French and British press.

That this idea should exist so strongly in the countries that wish to get more American loans and gifts is not surprising. What is much more strange is to find it endorsed by some American business men and even by some American economists.

Yet it is unadulterated nonsense.

If it were true that we could create prosperity merely by making goods to give away, then we would not have to give them to foreign countries. We could accomplish the same result by making the goods to dump into the sea. Or the Federal government could order the goods made to be given away to the poor in our own country. It could furnish them with free overcoats, free lunches and free automobiles; order any amount of new housing built, turn it over to them, and finance it by inflation or add it to the American taxpayer's bill. Simplest of all, it could turn over directly to American lower-income groups additional money taken from the taxpayers and let them buy with it whatever they themselves wanted. The goods, at least, would then remain in this country. Why confuse the issue by bringing in foreign nations and foreign trade?

It ought to be clear to the poorest intelligence that nobody can get rich by giving his goods away. What seems to confuse otherwise intelligent people when this proposition is applied to a nation instead of an individual, however, is the fact that

it is possible for particular firms and persons within the nation to profit by such a transaction at the expense of all the rest. It is true, for example, that persons engaged exclusively or chiefly in export business might gain on net balance as a result of bad loans made abroad. The exporter might profit at first by additional foreign sales. But if the foreign loan is not repaid, then those who make it lose the money. If it is a government loan, then the loss must be made good out of increased taxes on every American. American consumers will then have just that much less money left with which to buy American goods. For every extra dollar that the foreign buyers had been given to buy such goods, in other words, domestic buyers would ultimately have one dollar less. Businesses that depend on domestic trade would therefore be hurt in the long run at least as much as those engaged primarily in export business had been helped. Considered individually, American consumers would be impoverished by higher taxes. And considered collectively, the country would be poorer by the amount of goods it had given away.

So many confusions exist about foreign trade that it is possible here to call attention only to one or two of them that bear immediately upon the present issue. One frequent fallacy, for example, which is implied in the foregoing quotation from the *Eastern Economist*, is that the United States produces "a surplus above its own needs" and must find an "outlet" for this "surplus." Nothing, of course, would be more foolish than for a country continually to produce more than it needed. From the standpoint of the nation as a whole, exports are produced to pay for imports. A nation with a permanent surplus of exports (including both "visible" and "invisible" items) would be merely a nation that was giving its goods away.

Wherever the most effective division of labor exists, wherever a nation devotes itself to producing what it can produce better, cheaper, or more efficiently than other nations, and is content to buy from others in turn the things that they can make

cheaper, foreign trade follows as a matter of course. But it is a fallacy to suppose that a large export trade is in itself necessary to "provide employment" or to give "60,000,000 jobs." If some of these jobs make exports that are not ultimately balanced by imports, then the labor is merely being thrown away. It is like a huge WPA project, with the added disadvantage that whatever is produced by the work goes to foreign countries instead of remaining at home. If, on the other hand, the exports are balanced either immediately or ultimately by imports, then as many American jobs are "lost," or kept from coming into existence, by buying the imports (instead of home-produced goods) as were "created" in the first place by the exports. In an autarkic economy, the jobs that are lost by lack of exports are offset by the jobs provided to make substitutes for the goods that would otherwise be imported. It is not employment that suffers, but efficiency and consumer satisfaction. A sound two-way foreign trade is important from the standpoint of the efficient world division of labor and the maximum creation of wealth; but it is in the long run irrelevant from the standpoint of "providing employment."

It is true, however, that *changes* in foreign trade, and *temporary* export or import surpluses (using "exports" and "imports" broadly, to include all goods and services) are important from the standpoint of employment and business activity. An excess of exports, other things being equal, is "inflationary"; and an excess of imports is "deflationary." That is to say, an excess of exports, by making goods at home scarcer than otherwise, tends to raise home prices, while an excess of imports, by making goods more plentiful than otherwise, tends to lower home prices.

In a speech on May 8, 1947, Dean Acheson, Under-Secretary of State, estimated that our annual exports of goods and services to the rest of the world during 1947 would total \$16,000,000,000, an all-time peacetime high, compared with annual exports of about \$4,000,000,000 before the war. Against this,

he said, we were expected to import only about \$8,000,000,000 of goods and services. A later estimate, in the Midyear Economic Report of the President, published on July 21, gave a much larger figure of the export surplus: "The goods and services we provided to other countries [during the first half of 1947] ran ahead of what they provided to us at the rate of 12.7 billion dollars a year."

Now except for that part of it which is financed out of immediate taxation, this export surplus of \$12,000,000,000 a year is inflationary. It means that we are paying out \$12,000,000,000 a year in wages, salaries and profits for goods and services that we do not get. It adds \$12,000,000,000 to the excess purchasing power competing for the goods that are left. We are increasing the volume of money incomes in relation to the goods produced for domestic consumption.

OUR INFLATIONARY EXPORT SURPLUS

10. *Our excess of exports of goods and services has already caused a dangerous price rise, and cannot be maintained at the present unparalleled rate.*

The outside world's monetary demand, increased and made possible by our loans and gifts, has mainly impinged upon American foodstuffs. As a result the wholesale price of foodstuffs here—which would have been high even without this abnormal foreign demand—had risen by the week ended Sept. 20, 1947 to 259 per cent of the 1939 level, and was still rising.

The United States is now in the midst of a tremendous inflationary boom. It is of great importance that this inflation should be prevented from going further. Yet our government's foreign aid policy can only intensify it. The basic cause of the rise in American food prices as compared with the pre-war period has, it is true, been the increase in domestic monetary purchasing power, brought about by the wartime tripling of the supply of money and credit. But precisely when American

consumers have become most concerned about the *further* rise in food prices in recent months, the Federal government is expanding the very policy of food exports that has done most to cause that further rise.

The theory that we should create an export surplus by unsound governmental loans would be foolish enough even if we had unemployment and wished prices to go up; it becomes downright idiotic in a period of full employment and when everyone is already complaining about high living costs.

By building the export surplus to a level that cannot possibly be maintained, we run the risk of repeating the American economic slump that developed in 1920 when peacetime loans abroad, unparalleled up to that time, were suddenly seen to be unsound and as suddenly dropped. If we are to mitigate the unstabilizing effects of the present export surplus, we must begin a gradual tapering off now.

CHAPTER VII

CAN EUROPE'S "NEEDS" BE MEASURED?

11. *There is no scientific or objective way of measuring either Europe's "needs" for aid or our "available resources" for supplying it. The report of the Paris conference of sixteen nations does not solve this problem. Any total arrived at must be arbitrary or sheer guesswork.*

Two ideas have been tenaciously held in connection with American aid to Europe. One, embodied in the Marshall proposal, is that Europe ought to find out and tell us precisely how much it "needs," either in terms of specific goods or in over-all terms of dollars. The other, put forward by those who fear the possible dimensions of the Marshall plan, is that the United States ought to "make an inventory of the resources it has available to contribute," either in terms of specific goods or of dollars.

The mere effort to compile such inventories of "needs" or "available resources" will have an important educational effect, and therefore it cannot be entirely fruitless. But we will do well to recognize from the very beginning that there is no scientific or objective way of measuring either Europe's needs or our available resources for aid.

What standard are we to adopt, for example, in measuring Europe's "need" or "deficit" or "shortage"? Some pre-war level of European consumption? Are we to support Europeans in the pre-war style to which they were accustomed? Is the calculation to be based, then, on "minimum standards of health and decency"? How would we apply such "minimum" standards? As averages? If so, in order that everyone might get the minimum, Europe would be obliged to adopt a totalitarian

system of complete equality of personal or family incomes regardless of anyone's contribution to output. Under such a system the last incentive to restored production, except the threat of the firing squad, would be destroyed.

Would America, then, be expected to make up the deficiencies for all those in Europe who had less than the calculated minimums — while those in Europe who had more were allowed to retain that more? If so, the whole burden of making up such deficiencies would fall on Americans, and none on better-off Europeans. And if the problem is primarily one of relieving poverty and under-nourishment, what of the superior claims on our charity of India, Latin America, Africa, China?

It may be thought that the problem is more amenable to solution in terms of shortages of specific goods. But how are these shortages themselves to be measured? Shortages in relation to what? We should know from our own experience that price-fixing can create any conceivable number of shortages. Whenever the price of any commodity is held by government edict below the level that a free market would bring, there will be a shortage of that commodity. Production and supply will be discouraged, consumption and demand stimulated. It is impossible to know what the "real" shortage is when market prices are not free. If the supply of product X is short in relation to the supply of products A, B and C, this lack of balance may be wholly the result of government price-fixing. If a given product is short in relation to its pre-war supply, the first question that must be raised is whether that supply could not be increased by allowing the price to go up to stimulate production. The second question is whether it is in any case the duty of United States citizens to make up a European deficit of any product below its pre-war supply.

Such questions are enough to show that there is no scientific standard by which Europe's need for aid can be measured. Any "estimate" must be at best arbitrary, if not the sheerest guesswork.

THE SIXTEEN-NATION REPORT

THE REPORT of the Paris conference of sixteen nations in response to the Marshall proposal does nothing to shake this conclusion. Let us begin with the over-all estimates that these nations put out of their needs — or rather of what they call their combined prospective “deficit” — over the next four years.

The report places this deficit at the huge sum of \$22,440,000,000. Elsewhere in its text it mentions the need of some \$3,000,000,000 for currency stabilization loans. These appear to be outside the foregoing total. If we add them we get a grand total of \$25,000,000,000 as the estimate of the outside “needs” of these countries for the next four years. When we put on top of this some \$15,000,000,000 that the United States will have spent since V-J Day by the end of the present year in the attempt to rebuild Europe, it brings the bill to the staggering total of \$40,000,000,000.

How much validity do these “deficit” figures presented by the sixteen European nations really have? The original total that the sixteen nations arrived at, we must remember, amounted to more than \$29,000,000,000. (And this apparently did not include the \$3,000,000,000 estimate for currency stabilization.) Not until after our State Department privately protested that this sum was too large was it reduced to \$22,440,000,000. The estimate eventually published presumably meets our State Department’s demands, in that it is lower than the original estimate, and tapers down each year. But suppose our government does all that is now demanded of it, and Europe’s economy nevertheless still breaks down? Will we not be told that it was our fault — that our aid was “too little and too late” — that these were not Europe’s real estimates of its needs, but merely slashed figures put forward to conciliate the State Department and an “economy-minded” Congress?

Even apart from this, what reason is there to take seriously

these estimates of annual deficits? The report itself declares: "Unfortunately, the size of the problem has proved greater than was expected. The disruption caused by the war was more far-reaching and the obstacles to recovery more formidable than was realized even six months ago." But if the sixteen nations admit that they then failed to guess right even six months ahead, what reason is there to suppose that they are now guessing right four years ahead? And if (as we must suspect) the deterioration in those six months was not the result of a war that ended more than two years ago but of new factors, and primarily of the unsound economic policies followed by European governments in those six months, then the prospective European "deficit" could be either much greater or much less than the figures presented, depending upon the future policies followed.

It is impossible, moreover, for any nation to predict its future trade deficit by adding together its future "requirements" of specific goods. For such "requirements," as we have already seen, are arbitrary except in relation to some standard, and the standard adopted must itself be arbitrary. If there were some nation as much more productive than the United States as we are than Europe, we could no doubt submit a very impressive list of "requirements" to it, including veterans' housing, railway freight cars, steel, automobiles, and the principal foodstuffs and raw materials that we import, including sugar, coffee, rubber and wool.

There is no such thing, finally, as a predestined trade deficit independent of loans from outside, of internal inflation, of price-fixing, of tariff policies, of trade controls, of domestic production, of price levels and of foreign exchange rates.

To examine simply the first of these factors — loans from outside — it should be obvious that the economic causation is precisely the reverse of what the sixteen-nation report tacitly assumes. *It is only gifts, credits or loans from outside that permit a trade deficit to continue.* Otherwise the only trade

deficit that is possible is one that is paid for by the sale of foreign securities or foreign currencies previously held or by the direct shipment of gold. In the long run imports and exports balance, not because a nation's production goes up or down, or because some set of brilliant bureaucratic controls makes them balance, but simply, as John Jewkes of the University of Manchester has put it, as "the result of the insistence of people upon getting paid for what they sell." If we extend no further gifts or credit, the outside world cannot continue to have a trade deficit. *It is the loans and gifts themselves that will chiefly determine the size of the future European net trade deficit with us.*

EUROPE'S FOUR-YEAR PLAN

THE REPORT of the sixteen European nations is a skillful presentation of the case for heavy and immediate financial aid from the United States. Many Americans have been impressed by its diplomatic tone, its "painstaking" estimates, and its "calm and measured" language. But the more the report is examined the less assurance does it give that these nations are even yet prepared to abandon the economic restrictions that have been chiefly responsible for bringing on the present crisis.

Throughout the report there is constant emphasis on production "targets." We are told precisely how much bread grains, potatoes, sugar, meat and milk these countries intend to produce in each of the next four years; precisely how many tons of coal and steel, and how many kilowatt hours of electricity; precisely how much they intend to expand oil-refining capacity, inland transport and merchant fleets. We are proudly told that "these production programs, taken as a whole, represent an expansion of output similar in general scale to that achieved by the United States in the mobilization years 1940-1944."

There seems to be an implication here that to set a target is almost as good as to reach it. Surely the sad fate of the British

targets so confidently published in February of 1947 ought to have sufficiently underlined the difference between ardent hopes and cold realities.

The whole concept of government "production targets" is in origin totalitarian. It is part of the modern mania for imitating Russian Five-Year Plans — an imitation that is the sincerest flattery to Communism. Why should the Russian Communists doubt the superiority of their system when they see nearly all of Europe aping one of its basic features? For only under a collectivist concept is it considered the function of government officials to say just how much shall be produced of each major commodity. It is of minor importance that the guesses of the bureaucrats are almost bound to go wrong. Far more serious is the fact that the mere setting of government production targets is in effect a way of setting aside the free market, setting aside a free economy. It is a way of telling the consumers that the things that are produced, and the relative proportions they are produced in, are not to be determined by their own demands but by what government bureaucrats decide in advance is good for them.

The supreme irony is that the only country in the world today that is really producing anything — and for whose goods the rest of the world is therefore clamoring — is almost the only country that does not have government production "targets," but merely turns out goods in the volumes and proportions determined by supply and demand, free prices and free profits. But just as the rooster Chanticleer was convinced that the sun could not rise until he crowed, so European bureaucrats are still convinced that there can be no production unless they first of all set production targets.

Implicit in production "targets" is the whole system of price control, rationing, allocations, government licenses, prohibitions and decrees. There is no indication in the sixteen-nation report that this dictated economic system is to be abandoned, certainly not in the near future. Only once in the report is it

admitted that the system of price control "is likely to jeopardize production." But this delicate hint is not elaborated, nor is any conclusion deduced from it. Under present circumstances, the report assumes, "stability cannot exist unless it is constantly reinforced by controls and rationing."

In short, European bureaucracy still believes at bottom what our own OPA believed, that price control cannot be abandoned "until supply catches up with demand." What this overlooks is that artificially low price ceilings in themselves increase demand and reduce production and supply, so perpetuating the very shortage that they were designed to counter. In the European system almost the whole mechanism of economic self-adjustment has been destroyed. Neither prices nor wages nor exchange rates are free to move to the points where they can tell the truth about the ever-changing relations of supply and demand and restore equilibrium between them. The inevitable result is a chronic shortage of goods and a chronic trade deficit.

The only important elastic element left in the world is American prices, which must now bear the full brunt of world inflationary demand. And when they respond to the process of trying to take on this disproportionate function, an outcry is raised not to free the markets of Europe but to suppress market freedom even here. To the extent that this is done, we may be sure that we shall not only lose our economic freedom, but make shortages and rationing worldwide and permanent.

FOUR LINES OF ACTION

MANY commentators have been impressed by the "four lines of action" upon which the European recovery program is based. As presented in the report these four points are:

1. Starting production effort by each of the participating countries, especially in agriculture, fuel and power, transport, and the modernization of equipment.
2. The creation and maintenance of internal financial

stability as an essential condition for securing the full use of Europe's productive and financial resources.

3. The development of economic cooperation between the participating countries.
4. A solution of the problem of the participating countries' deficit with the American continent, particularly by exports.

As statements of goals, these points are beyond criticism. What country, indeed, would not wish to increase its production, to maintain internal financial stability, to get cooperation from other countries, and to terminate a condition of economic dependence on outside help? The real problem to be solved, however, concerns the *methods* likely to achieve these goals. And it is precisely here that the report gives most grounds for misgiving.

The report of the sixteen nations is not altogether without sections that give some reason for hope. One of these is the sympathetic discussion of customs unions. It is admitted, however, that at the moment such discussion is rather academic. The report itself reminds us that a customs union can only be achieved by "progressive stages over a period of years." What is perhaps not so well recognized in the report is that a customs union is impossible between controlled economies. To have really uniform tariffs the members of a customs union must have a uniform currency, or at least currencies freely convertible into each other in any amounts at fixed rates. The countries embraced in the union must also have uniform prices for commodities, differing only by transportation costs—which means that they cannot have separate price control, rationing or allocation systems.

Of more immediate bearing are the sections on inflation. The report contains the significant admission that "the growth of money incomes develops with cumulative force when it is fed by inflationary financing of budget deficits." It contains the definite promise of the French Government that "the year

1948 will see the end of all new borrowing from the Bank of France," and the promise of the Italian Government that "it will approve no new expenditure unless provision is made for revenue to a corresponding amount." These pledges are important. They should not be minimized. But it will not be easy to fulfill them. For they mean the imposition of unpopular taxes, and they probably mean also the abandonment or reduction of expenditures popular with powerful groups, such as those on food subsidies, nationalization subsidies, new social security schemes, and big government capital investment programs. It remains to be seen whether the governments of France and Italy will prove strong enough to carry out these pledges.

OUR "AVAILABLE SURPLUS"

HARDLY less difficult than determining Europe's "needs" is the problem of determining the "available surplus" of American goods for foreign aid. Is this surplus to be measured by whatever income we may have above the average European level? Is it assumed to be our duty to lend or give enough to reduce us to that level? Will the wealthier European countries then be equally willing to reduce their incomes to that of the poorer countries, and these in turn to the Asiatic level, until the whole level of world incomes is equalized?

If not, what is to be the standard for measuring our surplus? Is it to be measured in specific articles? But the articles of which we have a "surplus above our own needs" are for the most part the articles specifically made for export trade. If we simply give away those articles, then with what can we buy the articles that we need to import—such as sugar, coffee, tea, cocoa, wool, rubber, hides, silk, newsprint, and a thousand other raw materials or finished products? It is precisely with the proceeds from our surpluses that we make up for our shortages. We can, of course, give the outside world more food and

other products than it is able or willing to pay for with its own exports to us. But we can do so only by consenting to go with less ourselves, by submitting to higher taxes and by forcing up prices here, perhaps dizzily, as a consequence of reduced supplies.

The most impressive effort so far made at this writing to estimate the resources that we have available to help Europe appeared in former President Herbert Hoover's letter of June 15, 1947 to Senator Styles Bridges, Chairman of the Senate Appropriations Committee. This letter, without attempting to set exact limits to our contribution, showed what the serious effects on our economy had been of our contributions up to that date. It emphasizes some of the considerations that have just been outlined, in addition to summarizing the post-war contributions already made.

CHAPTER VIII

THE PROBLEM OF COMMUNISM

12. *Making heavy loans or gifts to European nations is not the most effective way to fight world communism.*

There is one argument for our policy of making huge loans and gifts abroad that appeals especially to American conservatives. It is that this policy is the only way to "halt the spread of communism" and that, if we allow Europe simply to stew in its own juice, it will surely go communistic. This is usually accompanied by the argument that if our loans, however large, succeed in stopping communism, or in reversing the trend to it, they will have proved very cheap.

When one tries to analyze this simple argument one finds that it begs all the real questions. In its usual form, it simply *takes it for granted* that loans to Europe will stop communism. The assumption is that wherever you have a country in which there is a powerful communist party and in which the government in power is non-communist, financial help to that government will stop communism. Just how it will stop it is not made clear. The mere *intention* on our part that the loans should be used to combat communism is commonly taken as an assurance that they must actually have that effect. The loans, it is apparently assumed, will make the recipient governments friendly and grateful to us; and by supporting them, by keeping them on their feet, by preventing starvation, we will make the communist ideology in those countries wane or die. Sometimes the loans, like those to Greece and Turkey, are deliberately intended to combat Russian aggression by adding to the military strength of the countries threatened by it.

It is obvious that we have more than one question to deal

with here. We have on the one hand the question of what is the most effective means to combat the communist ideology. We have on the other hand the question of what is the most effective means of curbing further Russian aggression which rests on Russian military power. The two questions are connected, but they are certainly not identical. The two ends require different means, though to the extent that we succeed in one it will of course help us with the other.

Clearly the burden of proof ought to rest on those who contend that making loans or gifts to Europe is the most effective means of combatting the communist ideology. At most, as many have already come to recognize, loans could be only a limited and temporary means for combatting the spread of revolutionary ideas. It would certainly seem at first glance much more effective, and incomparably cheaper, for our government to combat revolutionary ideas directly. It could do it directly by answering systematically the lies that are published in Moscow and in the communist press in this country and abroad about American intentions and about the "failures" of the capitalist system. It could take the aggressive in the propaganda war that Russia has launched against us, and bring before the United Nations (to cite but a single example) the horrors of "Gulag" — the Soviet Slave Labor Trust — with its more than 14,000,000 slave workers scattered in concentration camps through the length and breadth of Russia,¹ toiling twelve hours a day under conditions of unspeakable wretchedness, starvation and disease. Certainly, instead of weakening ourselves by turning resources over to highly unstable and unreliable European governments, it would seem better to expound directly the merits of our free enterprise system and to contrast them with the hunger, terror and slavery under communism.

The common argument that capitalism must provide even more goods than it already does, in order to prove its "superiority" over communism, is complete nonsense. The comparison

¹ See the documented map published by *Plain Talk* (240 Madison Ave., New York).

is already so enormously in capitalism's favor that no further demonstration of this superiority is needed. What is needed is to point out how great this superiority already is.

It may unfortunately be doubted whether our government, or any government, is the best instrument for this counter-propaganda in favor of capitalism. It is obvious that most of those in our government do not know what the arguments for capitalism, and against communism, really are. Their so-called defense of capitalism is usually apologetic. They are nearly always defending some other kind of capitalism than the kind we actually have. They are defending their own version of a capitalism "reformed" in accordance with their particular interventionist ideas.

But if the American government cannot be counted upon as the ideal defender of capitalism or the ideal critic of communism, much less, certainly, can most European governments to which our loans are being and would be made. Practically all these governments consist of "economic planners," that is, people who believe in a dictated economy, and who in a hundred ways are making it impossible for a free, competitive capitalism to function within their borders. Some of these governments consist of outright socialists, who do not believe in capitalism at all.

"FIGHTING" COMMUNISM WITH SOCIALISM

AND THERE could hardly be a more perverse and mistaken idea than the idea that you can fight communism with socialism. So-called "gradual" socialism is at best a halfway step toward communism. The economic ideals of socialism and communism are identical. Both believe in government ownership and operation of the means of production. Once this ownership and operation become sufficiently extensive, the government has economic life-and-death powers over the individual. It can say

where he must take his job, what job he must take, or whether he can take a job at all. And once the government has this power, the liberty of the individual has in fact, if not in form, disappeared. As Alexander Hamilton pointed out in the *Federalist Papers* a century and a half ago, "A power over a man's subsistence amounts to a power over his will."

Socialism and communism differ only in their political methods. The socialists, it is true, believe in coming into power by peaceful means, through the ballot. But even communists prefer a "peaceful" means wherever it is open to them. It is only where they cannot get into power by peaceful trickery and intrigue that they resort to open force. The socialists, it is true, talk of preserving the methods of democracy and the liberty of the individual, and most of them are no doubt sincere in their protestations. But they fail to recognize that in fact socialism does not and cannot permit economic liberty, and therefore in fact it must ultimately cease to permit any other important kind of liberty. A man's opinions must be such that they please the officials in power if he is to gain any promotion or even enjoy any security under socialism.

Under capitalism, in addition to the possibility of going into business for oneself, there are in the United States several million employers competing against each other for labor. Their competition not only raises the wages but protects the liberties of the worker. His situation becomes incomparably worse when he must bow to the will and terms of a single employer, the State. The history of the spread of socialism is in fact a history of the disappearance of peace, representative institutions, limited government, and personal liberty.

Moreover, as post-war experience has already shown, when American funds are turned over to socialist governments or to "planning" governments, recovery does not in fact take place. It is prevented by the very policies that these governments pursue. What the American funds accomplish is to make the dictated economy or socialism appear for a time to work better

than it actually does. The loss of these funds by the United States, on the other hand, by promoting inflation and increasing the scarcity of goods here, appears to make our capitalism work worse than it actually does. Nevertheless, in spite of this help to the dictated or socialistic economies, the borrowed funds continue to run out and the borrowing government is soon back for more. Meanwhile the communists have found an additional argument against the government that has failed to bring recovery. It has failed, they say triumphantly, not because it has adopted restrictive regulations and practiced socialism, but because its regulations have not been drastic enough and because its socialism has been partial and half-hearted. And the socialist and collectivist planners who have denounced free enterprise, and have taught the citizen that only government can solve his problems, have deprived themselves of any convincing answer to this assertion.

Once more we return to the conclusion that our loans or grants could bring at best a minor and temporary improvement in the economic conditions of any nation unless they were accompanied by drastic reforms in that nation. As the economist Wilhelm Röpke has put it: "Without a drastic internal reform of the national economy, to put an end to inflation and socialist controls, foreign credits can have no lasting effects, just as a man cannot be kept alive indefinitely by perpetual blood transfusions if the cause of his hemorrhage is not removed." And if this is what has already happened in the case of England, "whose dollar loan could not keep pace with the constant wastage of a socialist system which destroyed the price mechanism and its incentives," what are we to expect in the case of countries even more deeply infected by inflation and collectivism?

Moreover, it is not the actual level of economic welfare within a nation, but its dominant ideology, which really decides what course it will take. The belief that Europe will turn in desperation to communism unless it receives heavy financial help from our government rests on one or all of three assump-

tions. The first is that communism is more efficient than private enterprise in supplying at least the bare means of subsistence. The second is that free enterprise is a luxury that only an already prosperous nation can afford. The third is that, regardless of the truth of the matter, hungry and desperate people always *believe* communism to be more efficient than free enterprise. The first two assumptions are always false. The third is likely to be true only if communist propaganda is allowed to monopolize the field, or if the case for private enterprise is presented apologetically or stupidly. In Russia today, according to a recent study by the United States Department of Labor, the average worker is about *one-tenth* as well off as the American worker in terms of what his wages will buy. Compared with a year ago the prices of rationed foodstuffs in Russia have risen about 166 per cent, while the Russian worker's wages have risen only 25 per cent. Would "hungry and desperate" men be eager to embrace communism if they were made aware of such basic facts?

The argument that Europe will go Communist unless it gets huge loans or gifts from us takes more than one form. On its most naive level it is something like the threat of a poor relation to commit suicide unless he is given a handout. In its most plausible form the argument is that the Communists will capitalize on starvation and economic chaos in Europe by attempts to seize power. But this argument takes it for granted that loans from the United States will actually play the decisive role in averting hunger and restoring Europe's economy. The really decisive role, however, as we have already seen, will be played not by American aid but by the economic policies pursued in Europe itself. Unless European governments permit the restoration of a working competitive price mechanism, our future aid will be nullified as completely as was our loan to Great Britain.

ANTI-COMMUNIST POLICY

THERE remains to be considered the granting of frankly political loans, like those to Greece and Turkey, in order to support the military establishments of those countries and help them to combat any Russian or Russian-inspired effort at conquest or at a *coup d'etat*. It is beyond the purpose of this study to analyze in detail these more strictly political aims. But it may be pointed out that, if we are to adopt a policy of preventing or halting any Russian military advance or military coup, we must have the clarity and courage to see and accept all the implications of such a policy.

Political loans can be only a part of it, and moreover only a subordinate part. It is worse than useless to give to countries threatened by Russian domination less than enough to resist the threat. The resources that we have contributed would then soon become part of Russian resources to be used against our interest. If a country to which we have granted such aid subsequently seems in danger nonetheless of being conquered or controlled by Russia, then we must not only pour in further aid, but stand ready even to use our own direct military force if the aid we have already given is not to be turned against us.

We must also keep in mind the fact that the policy of military aid to foreign countries always involves the danger that the very government to which the aid has been granted may use it against us, or that that government may be overthrown either through an internal revolution or a "free" election within that country, after which the new government may proceed to use our aid against us.

When we make frankly political loans for basically military reasons, in short, we must not keep ourselves willfully blind to the dangers of these loans. Above all, our policy must be consistent. It is merely a piece of diplomatic imbecility to make military loans on the one hand to Greece and Turkey in order

to enable them to combat the threat of Russia, and then to turn around and beg Russia to come into a plan to accept loans from us for "economic rehabilitation" which would inevitably be used to maintain or increase her military strength. It is insane to strengthen Turkey to fight Russia and then offer to strengthen Russia to fight Turkey.

The Marshall plan was in origin a political *retreat* from the Truman Doctrine. In it all the military implications of the Truman Doctrine were dropped. Russia herself was invited to share in this new distribution of American dollars. Now that nobody can any longer doubt that Russia is waging a cold war on us, the Marshall plan is being presented in Washington as a logical development and application of the Truman Doctrine. It is presented as the American government's program for "containing" and combatting world communism. Unfortunately, the comparatively easy decision to give more of the American taxpayer's money away cannot be regarded as a substitute for the hard political and diplomatic decisions that any serious program of countering Russian Communist aggression must involve. The illusion that all we need to do to halt Russia is to give away money may divert us until too late from the steps we really need to take.

THE SUBSERVIENCE OF CONTRADICTION

THE FACT that Russia has spurned the invitation to participate in the Marshall plan, and that the "new" Communist International has denounced it, has, however, enormously increased the popularity of that plan in the United States. If Communist Russia does not like it, it is thought, it must be good. If Russia fears it, then it must have been a very shrewd political move, and we should drive ahead with it.

Before we too hastily make this crucial decision, however, it will be well to try to analyze with the utmost care the reasons why Russia opposed the plan. She could, after all, have em-

barrassed us tremendously by hailing the plan, putting in a request for \$25,000,000,000 or so as her own share of America's largess, proposed that Europe adopt communism to insure recovery under the plan, or at the very least insisted that there must be no interference on our part with her communistic policies in exchange for our loan. Such tactics would have put Secretary Marshall in the dilemma either of having to offer Europe and Russia fantastic sums without even getting in return policies that might help recovery and world peace, or of turning down the plan and opening himself to the Russian accusation of having made a fraudulent offer and welshed on it.

If the noisy Russian opposition to the Marshall plan is not simulated but sincere, then the Russians may have made a grave error which has needlessly alienated them from the Western countries that look to us for help. One possible reason for this error is that the Russian economists sincerely hold the nonsensical doctrine which was reflected in Pravda of June 25 (and which has its roots in fact in the preachments of Marx and his disciple Lenin) that a capitalist country desperately needs to "conquer" foreign markets for its "surplus products"; and that the Marshall proposal to give Europe money will help us get rid of these "surplus" goods and so prolong the American boom and postpone, perhaps indefinitely, the "ripening economic crisis" here. As we have already seen this view to be grossly fallacious, it would be the worst of all reasons for driving ahead with an inflationary loan policy.

Another possible explanation of such a Russian error would lie in the propensity of the Kremlin to ascribe to us the same kind of motives and tactics that inspire its own policies. It is Russian policy, for example, to give as little help as possible for as great control as possible. When the Kremlin gives "economic help" to a neighboring country, it consists usually of 1 per cent help and 99 per cent propaganda glorifying that help. If Russia had offered an equivalent of the Marshall plan, the dominating purpose of the offer would certainly have been

an extension of Russian political control and influence. The Kremlin leaders therefore may have taken the Marshall plan to be essentially a plan for increasing American dominance, prestige and military power and alienating the satellite States from Russia. They attached so much importance to this danger that they threw away the opportunity of exploiting the Marshall plan for their own purposes as they might have done. But as the Marshall plan is in fact what it professes to be—an offer of large American resources in return for no controls whatever, and only for the conditions suggested by the borrowing nations themselves—Russian suspicions would hardly seem sufficiently warranted to justify unqualified endorsement of the Marshall plan by Americans.

The foregoing assumption regarding the Kremlin's interpretation of the Marshall plan may be correct. There is some ground for it in the language of the manifesto issued on October 5 by the revived Communist International. This explicitly denounces, not the Marshall plan, but something that it calls "the Truman-Marshall plan"—which implies that in the Russian view the Truman Doctrine and the Marshall plan are identical.

But these assumptions regarding the Russian government's real beliefs could be mistaken. If we have learned anything in the last thirty years about Communist methods, we are safe in assuming that the Vishinsky United Nations speech, the open revival of the Comintern, and all other recent Russian steps, are the outcome of plans long worked out — probably before either the Truman Doctrine or the Marshall plan was even thought of. *Any* policy we had contemplated or decided upon would have been denounced. The purpose of this Russian Communist campaign is simple. It is to discredit America; and therefore everything we do or think of doing must be discredited. Totalitarian propaganda is total: it makes no distinctions. Nothing would suit the Russian book better than a withdrawal of all American troops from Europe tomorrow; and

yet if we did this, the Russian propaganda machine would doubtless tell Europe, after our action had been taken, that once more the United States, interested only in holding on to its own dollars, had left Europe in the lurch, as the result of a secret deal made with the Hitlerites and German militarists.

It would be a profound mistake, therefore, for the United States to drive ahead with the Marshall plan simply because the Communists have denounced it. This would be merely "the subservience of contradiction." If we followed such a course consistently, the Communists could make us adopt any policy they pleased merely by advocating its opposite.

Is the Kremlin so stupid as not to know the effect of its opposition? Is it so stupid that it does not realize that the best way to assure American persistence in the Marshall plan is to have the Communists everywhere denounce the plan precisely as they are doing? This would be a dangerous assumption for us to make: like that of a chess player who smugly assumes that an astute opponent has made a very stupid move, and then makes the "obvious" reply—which turns out to be precisely the reply that his opponent hoped for, and the reply that may cost him the game. A good chess player, when his opponent has made what appears on the surface to be a merely stupid move, gives far more thought than otherwise to the purpose of that move and the possible consequences of his own reply.

We should do the things that really counter the Russian menace, and not merely the things that the Russians publicly say they don't like.

Certainly we should not overlook the fact that the Communists have politically a very strong issue here. This, as reflected in the text of the October 5 manifesto, is the call upon all Communists in Europe to "grasp in their hands the banner of national independence and sovereignty in their own countries," and "to fight against attempts at the economic and political subjugation of their countries." Can we afford to feed the Communists the ammunition they want for this propaganda?

Once more we are brought back to a central dilemma of the Marshall plan: if our loans are made without economic reforms in the borrowing countries, the funds will be dissipated without bringing any revival; but if we insist on reforms as a condition for our loans, the Communists will exploit the powerful issue of "dollar imperialism" and "economic subjugation."

The Communists, finally, may be able to counter the Marshall plan not merely with propaganda, but with direct action. As James Reston has pointed out: "It is not difficult to see what the Communists, with their power over the labor unions in France and Italy, could do to the Paris reconstruction program, even if the United States Congress voted the full \$22,440,000,000 requested by the sixteen-nation conference."¹

¹*New York Times*, October 7, 1947.

CHAPTER IX

YOU CAN'T BUY GOOD WILL

13. *It will be a profound mistake to count on gratitude, or to believe that we are purchasing any permanent good will by government loans and gifts to Europe.*

It should be sufficient to remind ourselves that we did not get gratitude or good will from the Yugoslavian government in return for the millions of dollars worth of supplies poured into that country by UNRRA, and that we did not get it from the Russian Government even in return for \$11,000,000,000 of Lend-lease, extended at a time when it meant the very survival of Russia.

Nor is it from communist-controlled countries alone that our financial help has failed to buy gratitude or good will. Passing over the effect in this direction of the \$30,000,000,000 of American Lend-lease to Great Britain, the whole amount of which was written off, we need merely consider the response to the special post-war loan to Britain of \$3,750,000,000. Far from hearing continual grateful references to this in Parliament and in the British press, we hear constant resentment about its alleged "onerous" terms. (And, indeed, as it is impossible in the long run to work an economy half "planned" and half free, even a moderate requirement like sterling convertibility broke down, though it is essential to multilateral trade and much more in England's ultimate interest than in our own.)

When the terms of the American loan to Britain were first announced, even the dignified London *Economist* wrote: "If the purpose of the American Congress which decides American policy is, as it often seems to be, deliberately to wound and afflict the British people, it has certainly succeeded. It is

aggravating to find that our reward for losing a quarter of our national wealth in the common cause is to pay tribute for half a century to those who have been enriched by the war." The London *New Statesman* thought the loan a "disastrous bargain," and added: "We run grave risk of ultimately being compelled to invoke all the ingenious 'escape clauses' in the Agreements and of becoming an insolvent debtor. . . . Since everything points to Britain being compelled ultimately to repudiate commitments whose fulfillment United States trade policy will make impossible, we must face the probability of a future quarrel with America, and unrestricted commercial warfare." As late as July 19 of this year, Ernest Bevin, the British Foreign Secretary, appealed to the coal miners to keep Britain "out of the money-lenders' grip."

One could continue to quote ad libitum such adverse European comments on the effect of our help. Today the United States has become the scapegoat for politicians in virtually every country that has received grants from our government. Either our help, in their opinion, has been too paltry compared with their country's real needs, or it has been accompanied by onerous, humiliating or unworkable conditions. These conditions, it is always implied or stated, were imposed not to help revival in the aided country but for some narrowly selfish reason of our own capitalists or militarists. Even conservative foreign politicians blame us for giving credits which have helped to maintain socialist governments in office.

How, in the face of such a record, can any Americans still think that inter-governmental foreign loans buy the good will or friendship of the governments and people to whom they are made?

Gratitude, certainly as between governments, has been correctly defined as "the lively expectation of *future favors*."

CONFUSION OF PURPOSE

14. *Inter-governmental peacetime loans become ambiguous and confused in purpose.*

It is beyond the scope of this study to consider the wisdom of loans, gifts or other aid from one government to an allied government in time of war. This question raises political and military issues which must be dealt with on their own merits. But once the war has been successfully terminated, the primary reasons for such loans or contributions terminate with it. A few inter-governmental transactions may be necessary to take care of conditions growing directly out of the war or to liquidate the war alliance. But once this has been done, the continuation of inter-governmental loans in peacetime for peacetime purposes raises questions of an entirely different nature.

During a war, the purpose of inter-governmental war loans is clear: it is to keep one's allies in the war and to make their contribution to victory as great as possible. But the purpose of inter-governmental *peacetime* loans is certain to become confused. Few Americans are clear in their minds today regarding precisely what the central purpose is of our government's program of foreign aid.

Is it to relieve starvation and poverty? Then people in India, Africa, China, and parts of South America may need our help far more than people in Europe do.

Is it to halt communism? Then we must coldbloodedly distribute our help, not to the points at which it relieves the greatest human distress, but to the most strategic points to hold against communism. We must first of all ask ourselves, indeed, whether in a fight against communism loans to wobbly European governments are really our most effective weapon.

Is the purpose of our aid to meet a European economic crisis? Then the first thing to do is to ask what has caused the crisis.

And in this case too we must ask whether loans are the most effective method of dealing with it.

Is the central purpose of our aid merely to increase our export trade and to create prosperity? Then we must ask ourselves whether on these grounds the program makes any sense at all.

The Export-Import Bank was originally set up in the belief that it would promote foreign trade by making loans to foreign buyers. Whether a government institution was really needed or justified for this original reason we need not here inquire. It is enough to point out that the operations of the Export-Import Bank have drifted insensibly from commercial loans to political loans and then to thinly disguised relief.

When President Truman on March 12, 1947, made his first appeal to Congress for a loan of \$400,000,000 to Greece and Turkey, he rested his appeal frankly on the argument that "the very existence of the Greek state" was being "threatened by the terrorist activities of several thousand armed men, led by communists." He told them that Turkey needed financial assurance "for the purpose of effecting that modernization necessary for the maintenance of its national integrity," and that "we shall not realize our objectives unless we are willing to help free peoples to maintain their free institutions and their national integrity against aggressive movements that seek to impose on them totalitarian regimes." His reference to our government's protests "against coercion and intimidation, in violation of the Yalta Agreement, in Poland, Rumania and Bulgaria" left no doubt that his program was directed against aggression by Russia.

But by May 13—apparently in order once again to appease Russia and those Americans who were declaring that the "Truman Doctrine" led to war—Secretary Marshall was saying in an overseas broadcast: "There has been much of misunderstanding regarding our program of aid to Greece. There has been much of distortion and misrepresentation of our purpose.

We are answering the call of a valiant ally who has suffered much. . . . It is as simple as that."

But if it was as simple as that, why had the President gone out of his way to raise so much needless hostility in the first place?

Secretary Marshall's statement did nothing to lull the suspicion or hostility of Russia, but it apparently helped to confuse our own policy to such an amazing extent that we were soon inviting Russia herself to ask for loans from us! To paraphrase Santayana's definition of fanaticism, we redoubled our lending efforts after we had forgotten their aim.

AGAIN: THE DILEMMA OF CONDITIONS

15. *Inter-governmental loans raise insoluble dilemmas regarding the imposition of conditions.*

Inter-governmental loans, as we have already seen, are on the horns of this dilemma. If on the one hand they are made without conditions, the funds are squandered and dissipated and fail to accomplish their purpose. They may even be used for the precise opposite of the purpose that the lender had in mind. But if the lending government attempts to impose conditions, its attempt causes immediate resentment. It is called "dollar diplomacy"; or "American imperialism"; or "interfering in the internal affairs" of the borrowing nation. The resentment is quickly exploited by the Communists in that nation. The bitter comments we have already quoted from the *London Economist*, on the "crippling" and "intolerable" conditions of the American loan to England, show that the resentment is felt also by supposedly responsible opinion in the borrowing nation.

The dilemma is, in fact, inherent. It lies in the attempt of one government to bribe another into following economic policies which that other government does not believe in sincerely enough to follow without the bribe. The dictation must be

resented even if accepted. The people in the borrowing nation are led to feel that they have sold their economic birthright for a mess of pottage. Everything that goes wrong is blamed on the conditions of the loan. The ill will caused by this is in itself enough to offset any good will that the loan might otherwise have brought.

Many people still suppose that this dilemma was escaped by the so-called Marshall plan. Under that plan the American government has not ostensibly dictated any conditions whatever. It merely asked the borrowing governments themselves to set forth a program of self-help before the loans were extended. But the dilemma was not escaped. For the report of the sixteen nations shows that they have no intention of abandoning the major policies which have brought them to their present crisis. They will continue as before to impose price control and exchange control, food subsidies, cheap money, ambitious capital investment programs, government-dictated production, nationalization and socialism. Naturally. For these policies that distort and paralyze the economic process are the very ones that were adopted in the belief that they promote recovery. And not less important, most American government officials themselves seem to think that these policies are necessary and good. They have, in fact, imposed most of them on Germany and Japan. How, then, can we expect them to be reversed?

RESTORE PRIVATE LENDING

16. *All this must lead us to the conclusion that the business of international lending should be returned to private hands.*

Before the First World War, and even after it, international lending meant loans made by private investors in the expectation of profit. "Freedom of international trade" meant the freedom of private individuals to buy and sell, lend and borrow,

in whatever market they chose and wherever they found it most advantageous to do so.

When international loans are made by private lenders, either to governments or to private firms or projects, the dilemmas we have been discussing disappear. In private transactions commercial considerations are certain to dominate. Loans will be made only if the lender has good reason to believe that the borrower intends to repay the loan and will be in position to do so. They will be made only for projects that promise to pay their own way. All this follows from the fact that the private lender is risking his own funds, and wishes to make sure that his capital is safe. Capital invested in projects that pay for themselves assures that world resources are being most efficiently utilized and that borrowed capital is being used in the ways that do most to promote production.

Of course private lenders are not omniscient. They do make mistakes. After the First World War private international lenders made some bad ones (though not as big or as bad as our government made). When private lenders err, resources of labor and capital are misdirected and at least partly wasted. But nobody had to buy the unsound foreign bonds floated in this country after the First World War. Private errors are, indeed, kept down to a minimum by the fact that people are risking their own funds. Those who lose cannot indefinitely continue to make such mistakes. Their money is gone. It is only those who have shown good judgment who have more funds for more investment. When a private lender makes a mistake in lending he pays for it himself. When a government official makes a mistake in lending the rest of us are forced to pay for it.

The private lender does not "impose conditions" in any direct sense. If he is a banker to whom a foreign government has come for a loan, there are times when he must simply tell that government that as long as it continues certain policies he is afraid American investors will not be interested. This is

not because investors have any desire to control the policies of that government, but because they wish assurance of repayment. Unsound policies do not provide that assurance.

The reforms brought about in the effort to conform with the wishes of private lenders are nearly always sound reforms. They are the kind of reforms that make for private or governmental solvency. They are not the kind of reforms imposed by one set of governmental planners upon another set of governmental planners. They do not mix politics with economics. They are reforms that anyone in any nation should welcome, because they give increased confidence that loans will be repaid.

When an American government official decides to grant a loan to Ruritania, on the other hand, it may be for any number of reasons. He may decide that this is necessary to carry out some political policy that he thinks is good. He may decide that it is "America's duty" to lend or give money to Ruritania. He is not, it is important to observe, giving his own money for such reasons. He is deciding that, in accordance with his judgment, A and B and C must be coerced into paying higher taxes so that these may be turned over to Ruritania.

It becomes a nice problem to decide whose charity this coerced charity really is. Is it the charity of the government official who is being so liberal with other people's money? Or is it the charity of A, B and C, who contributed the money not by their own voluntary choice but because it was seized from them by their own government to turn over to Ruritania?

It is commonly said that private capital is "inadequate" to take care of the present world crisis. This argument is of course untenable. Governments have ultimately no funds but the funds they take, directly or indirectly, from individuals and business concerns. Government capital is not a net addition to private capital; it is merely the portion of private capital that the government has seized for its own uses.

Another argument often put forward against private capital is that, under present conditions, only the most minute amounts

of private American capital would be loaned to Europe. But if it is true that private capital today would be lent abroad only in comparatively small amounts, it is for very good reasons. The long and shocking record of government repudiation, of exchange control, of expropriation and paralyzing restrictions, of prohibition of export of gold and export of capital which has made private lenders so distrustful, should certainly make us no less distrustful of the fate of money loaned by our government. International private lending will be restored when governments have taken the measures necessary to restore confidence. And it is of the first importance that at the earliest possible moment they should be made to take these measures.

INTERNATIONALISM: TRUE AND FALSE

THOSE who oppose heavy loans and grants from our own government to European governments are sometimes accused of being "isolationists." But those who believe that, in place of government loans, the barriers should be removed to private loans, and that our private lending markets should be freely opened up to foreign borrowers, are in fact the true internationalists. They see economic internationalism as the freedom of individuals in all lands to deal freely with each other, to buy from and sell to each other, and to do all this without having to run to some nationalistic-minded government bureaucrat for a special license for every transaction.

It is a completely false internationalism that sees dealings between nations as primarily dealings between the governments of those nations, as dealings between different groups of nationalistic bureaucrats, each preventing their own citizens from buying in the cheapest market, selling where they can sell most profitably, lending where their capital can be wisely used and properly safeguarded, and being allowed to indulge their own charitable instincts instead of those of the bureaucrats in charge of them.

It is a false internationalism which can only interpret "international cooperation" as meaning that the United States must be the perpetual innocent Candide among nations, or must act toward other nations like a rather soft-headed Santa Claus. It is a false internationalism that looks upon "cooperation" as a wholly one-sided affair in which one nation must lend or give without having anything to say about how its loans or gifts shall be used. It is a false internationalism that ignores or represses the freedom of individuals in one nation to buy or sell, lend or borrow, or cooperate as they please with individuals in another nation. It is a false internationalism that assumes it to be the responsibility of the government, rather than of the individual importer, to get the foreign exchange necessary to make his purchases.

In all former periods, when foreign exchange became scarce, importers simply paid a higher price in terms of their own currency to get hold of it. Today, as a result of carrying wartime practices over into peace, governments assume it to be their own responsibility to get foreign exchange for their importers; but when, as a result of over-buying abroad or inflation at home, or both, the dollar or any other foreign currency becomes scarce, the government not only refuses to pay anything more than its "official" price to get it, but forbids its importers to do so.

Would there be more "cooperation among the States," or less, if New Jersey, instead of allowing its citizens to trade as they pleased with the citizens of New York, Pennsylvania and Ohio, decided that it was losing too many dollars to New York, put a ban on the export of dollars from New Jersey, put a ceiling on New Jersey imports from other states, forbade its own citizens to buy what it called luxury imports, subjected every import or export to special license, prohibited its own residents from spending more than \$50 a year in travel outside the State, and then asked the Governor of New York to pass a

law forcing every New York taxpayer to contribute to a State loan to New Jersey?

This sort of thing, which now parades as “international co-operation,” and has the stupidity and effrontery to call the advocates of a free world economic system “the New Isolationists,” is not internationalism at all. Its true name is statism. Its true goal is totalitarianism. Its true end is world impoverishment and the suppression of individual liberties.

A POSSIBLE BRIDGE

17. If it is thought necessary to provide public stopgap or emergency credits until the processes of private international lending can be fully resumed, then the best instrumentality for making loans to bridge such a gap would be the existing International Bank for Reconstruction and Development, under a modified charter. But this should be turned into an emergency institution only, and not authorized to make new loans beyond the next five years.

Several arguments will no doubt be advanced against the view that we can stop foreign lending by our government and by government institutions and switch over to private lending *immediately*. It may be urged that it will take time to organize private lending and to turn lenders and borrowers from a government-lending psychology back to a private-lending psychology. It may be argued that, just as it was necessary to make Lend-lease contributions to our allies to keep them in the war and to make their contribution to victory most effective, so it will be not merely just but far-sighted on our part to extend to our former allies—or at least our potential future allies—enough help to allow them to restore their peacetime economies. It may be contended that though a currency stabilization loan to a foreign country might entail too much risk for private capitalists, the general economic gains to this country and to the world which would follow stabilization loans if they turned

out successfully would warrant this risk on the part of a government institution.

We have already indicated reasons for doubting the soundness of such arguments. They rest on the assumption that a loan would in fact be safe which would not be regarded as safe by people risking their own funds. Or they rest on the alternative assumption that a loan that would not be repaid would nevertheless stabilize the borrowing country's currency at the chosen parity. But no nation's currency can at once be free and stabilized unless that nation has won the confidence both of foreign owners of capital and of its own; and it cannot win this confidence unless it repays what it borrows. The assumptions on which the above reasoning rests are, in short, self-contradictory.

If, nevertheless, such reasoning prevails, the first problem to present itself would concern the most appropriate public institution for making stopgap loans of the type suggested. Proposals have been put forward for setting up an entirely new institution to make the contemplated loans under the Marshall plan. Yet one of the most troublesome features of the present situation is the multiplicity of governmental institutions already competing with each other to perform the same function. Students of bureaucracy will find nothing new in this: its whole tendency is to spawn ever-new overlapping agencies and create ever-new duplicating jobs.

For the purpose of making loans or grants to European governments, we have (surviving the now defunct Lend-lease and UNRRA), the Export-Import Bank, the Commodity Credit Corporation, the International Monetary Fund and the International Bank for Reconstruction and Development. In addition, the Treasury Department has acted as the agency to administer the loan to Great Britain. That ought to be about enough government foreign lending agencies without thinking up still another.

Of the two international institutions, the Fund in its present

form ought not to exist at all. Its managers are virtually without power to insist on internal fiscal or economic reforms before they grant their credits. A \$25,000,000 credit granted by the Fund to France, for example, is being used to keep the franc far above its real purchasing power and at a level which encourages imports and discourages exports. This merely prolongs the unbalance of French trade and creates a need for still more loans. Such a use of the resources of the Fund not only fails to do any good, but does positive harm.

The International Bank also lacks clear power to insist on reforms. As distinguished from the Fund, however, it at least has power to refuse loans unless the borrower is "in position to meet its obligations." And if stopgap loans of the type suggested above are to be made, then the already existing International Bank, with suitable revisions in its charter, would seem the most appropriate instrumentality for the purpose.

This could be thought of as an institution for emergency repairs to the financial damage done by the war. As such, it has several great merits as compared either with the International Fund or with our own government. It is compelled to take credit-worthiness into account because of the fact that it must sell its debentures to private investors. Having this excuse, and being an international institution, it could impose conditions on foreign governments with far less danger of arousing resentment than if our own government made the attempt. The American Secretary of the Treasury himself declared, in speaking before its first annual meeting on September 27, 1946, that "the International Bank must now assume the primary responsibility for underwriting reconstruction loans to countries otherwise unable to borrow on reasonable terms." But if the primary responsibility is now the Bank's, it has ceased to be that of the American government.

After the First World War, two types of non-private loans, as W. Randolph Burgess has pointed out, were effective—the central bank stabilization loans and the League of Nations

loans. They were effective because each was preceded by a thorough review of the position and program of the borrowing country. The loans were accompanied by expert aid and supervision. The granting of the credit thus became itself an assurance to the world that an effective program had been adopted. Big results were obtained with moderate means. In fact, the total of the nine League of Nations loans for recovery and stabilization made to six different countries was only £81,000,000, or somewhat less than \$400,000,000.¹

If the International Bank sends an expert economic mission to each country that applies for a loan, if it frankly tells each borrowing country that investors will not be interested unless that country makes certain specified economic reforms, then a loan may really achieve its purpose. Under such conditions, in fact, as experience with the League of Nations loans proved, it is not the loan itself that is important in assuring recovery, but the reforms made in order to get the loan.

Candor obliges us, however, to notice an important and perhaps decisive distinction between the Financial Committee of the League of Nations and the present International Bank. The League loans were controlled by governments that still believed in free enterprise and the gold standard, and insisted that the borrowing governments make reforms in that direction. The International Bank today is controlled at least in part by socialistic governments who think that "managed" paper currencies are not only just as good as gold but better. Is such an institution likely to insist on reforms that will really restore confidence and bring revival and stability?

Even under the most favorable assumptions, it is difficult to see how the International Bank could serve any useful purpose beyond a reasonable period of emergency. It should not be authorized to make new loans beyond the next four or five years—and perhaps even during that period provision should be

¹ Cf. "The League Loans", by Margaret G. Myers, *Political Science Quarterly*, December, 1945.

made for a gradual tapering off of the authorized volume of new loans.

If the International Bank, in brief, continues to be used at all, it should be as a temporary instrument to facilitate the transition to private international lending and not to delay or prevent it.

CHAPTER X

SUMMARY AND CONCLUSIONS

LET US begin by recapitulating the principles and conclusions we have reached so far:

1. As the United States produces only 12 per cent of the world's food supply, it is clear that America cannot feed the whole world.

2. The need for outside help to restore Europe's capital structure has been greatly exaggerated. Its unused resources for creating its own capital are very great.

3. Help from outside to any country goes eventually to relieve the *least* urgent needs which the government of that country then decides to meet.

4. Food relief and financial help from the United States will be futile unless the country aided discontinues policies which unbalance its trade and discourage or prevent production.

5. As a contribution to revival, the economic policies followed by a country are much more important than any foreign loan.

6. The United States cannot consistently recommend sound policies to foreign governments as a condition for loans, when it is not following such policies itself. It can preach effectively only by example. And it can do more for world revival by making its own economy sound and strong and free than by trying to put temporary props under economies built on the treacherous foundations of totalitarian controls.

7. Inter-governmental loans increase and prolong governmental restrictions on the economy both in the borrowing and in the lending country.

8. The bulk of our past and prospective government "loans" to foreign governments are little better than thinly disguised gifts.

9. It is not true that the United States needs foreign loans to keep full production and employment at home. It is not true that we can get rich by giving our goods away.

10. Our excess of exports of goods and services has already caused a dangerous price rise, and cannot be maintained at the present unparalleled rate.

11. There is no scientific or objective way of measuring either Europe's "needs" for aid or our "available resources" for supplying it. The report of the Paris conference of sixteen nations does not solve this problem. Any total arrived at must be arbitrary or sheer guesswork.

12. Making heavy loans or gifts to European nations is not the most effective way to fight world communism.

13. It will be a profound mistake to count on gratitude, or to believe that we are purchasing any permanent good will by government loans and gifts to Europe.

14. Inter-governmental peacetime loans become ambiguous and confused in purpose.

15. Inter-governmental loans raise insoluble dilemmas regarding the imposition of conditions.

16. All this must lead us to the conclusion that the business of international lending should be returned to private hands.

17. If it is thought necessary to provide public stopgap or emergency credits until the processes of private international lending can be fully resumed, then the best instrumentality for making loans to bridge such a gap would be the existing International Bank for Reconstruction and Development, under a modified charter. But this should be turned into an emergency institution only, and not authorized to make new loans beyond the next five years.

A POSITIVE PROGRAM

THIS resumé will serve as a reminder of the principal points in the course of the preceding argument. The argument has in the main necessarily been negative: it has sought to show that the proposed program of huge loans from our government to European governments will not only fail to achieve the results expected from it but may defeat the very ends its most disinterested advocates have in mind.

There are many readers, however, who will call for a more positive program. If loans from our own government to European governments are not the solution to world communism and economic chaos, they will ask, what *is* the solution? Such a problem is obviously too big to be answered in detail within the limits of a study of the present size, even if its author had the presumption to attempt a complete answer. One is sometimes disposed to wonder, indeed, what *can* be done to save people who are determined to have dictated economies and socialism, what *can* be done to save nations that are bent on destroying themselves.

In the course of the foregoing argument, however, "negative" as it is in its main contentions, a few positive recommendations have been explicitly stated and others have been necessarily implied. Perhaps it will help many readers if I merely list here in outline some of the main points which I believe ought to be a part of any positive program. The order in which the points are presented is not necessarily the precise temporal order in which they ought to be put into effect or the order of their inherent importance.

1. Make our own capitalism free and strong. Remove the government wartime controls that still hamper output and free markets. Strengthen especially the incentives to production.

2. Lower our own tariffs immediately, whether other nations do so or not.

3. Drastically revise our economic policy in Germany and Japan. Permit the Germans and Japanese themselves to restore their economies. Prohibit production only of direct weapons of war (for all production of any kind is of *potential* use in war) and stay to see that the prohibition is effective. Stop imposing socialism and Schachtism on Germany and Japan. Remove all strangling restrictions and restore incentives to output. Impose workable income reparations (not further capital seizures) to make our former enemies help the rest of the world instead of our having to support them.

4. Insist that the International Monetary Fund make two immediate minimum reforms: (a) remove the compulsion on all member nations to control exchange rates; (b) give the Fund managers power to impose conditions on borrowing governments. If these two reforms are opposed in other nations, either outright or by dilatory tactics, withdraw from the Fund altogether.

5. Return to a real instead of a merely technical gold basis for our currency.

6. Invite all nations to cooperate in returning to a world gold standard. Hold general or individual conferences with other governments to fix appropriate and maintainable parities, preferably related to each other in round figures.

7. Open our markets freely to foreign loans. Remove any unreasonable SEC requirements or other legal barriers.

8. Revise the charter of the International Bank to permit it to make stabilization loans under suitable conditions to countries contemplating eventual return to a gold standard. Make the Bank a short-lived emergency institution only.

9. Accept frankly the ideological and diplomatic challenge of Communist Russia. Defend capitalism without apology; attack the entire foundation of the Russian slave system. Recognize at last that appeasement of Stalin has been and will be as disastrous as was appeasement of Hitler.

10. Expose the fallacies of European statism and socialism

by our own contrary example. Do not attempt to impose free enterprise on Europe either by coercion or by bribes. But if we can't preach free enterprise to Europe, let us at least show the folly of a bankrupt Europe's trying to preach socialism to us.

11. Respond generously as individuals to every justified European appeal for help.

12. If overriding emergency seems to demand it let our government *give* food (not money) to Europe. Demand no government reforms in exchange for it; but stamp an American flag, literally or figuratively, on every package. Insist that Americans administer or share in administering the distribution abroad. Make sure that the food is distributed in accordance with individual need rather than with any European government's special political designs. Make sure that every European *knows* where the food comes from, and knows that it is a free gift without strings. Make sure that Communist lies about our aid will have a minimum political effect.

APPENDICES

APPENDIX A

AMERICAN POSTWAR AID EXTENDED OR STILL AVAILABLE TO FOREIGN COUNTRIES

(In Millions of Dollars)

	Available or potentially available	Funds drawn through June, 1947	Unutilized
U. S. GOVERNMENT LENDING			
Export-Import Bank loans	3,500	1,770	1,730
Lend-lease "pipeline" credits	1,500	1,250	(a)
Surplus property credits	1,150	900	250
Ship sales credits	210	110	100
Loan to United Kingdom	3,750	2,050	1,700
Monetary stabilization credits	287	9 (b)	278
INTERNATIONAL INSTITUTIONAL LENDING			
International Bank	3,266 (c)	100	3,166
International Fund	3,500 (d)	58	3,442
U. S. GOVT. RELIEF AND SPECIAL AID			
UNRRA	2,700 (e)	2,700	—
Post UNRRA relief	350	—	350
Relief in occupied areas	1,645	1,000 (e)	645 (f)
Greek-Turkish aid	400	—	400
Philippine aid program	695	170 (g)	525
Internat'l Refugee Organization	74	—	74
GRAND TOTAL	23,027	10,117	12,660

(a) Shipments held up, balance not likely to be utilized; (b) As of March 31, 1947; (c) The U. S. capital subscription of \$3,175 million plus dollars paid in by other countries through March 31, 1947. The authorized lending power of the Bank is \$8 billion; (d) The U. S. quota contribution of \$2,750 million plus gold paid in by other countries, partly estimated; (e) Estimated approximate cost; (f) Estimated expenditures in the President's budget for the fiscal year ending June 30, 1948; (g) \$100 million made available in surplus materials.

SOURCES: Assembled from miscellaneous sources including Export-Import Bank reports, Daily Statement of the U. S. Treasury, Treasury Bulletin, Survey of Current Business, reports of the International Bank, Budget for the fiscal year ending June 30, 1948, etc.

Compiled by The National City Bank of New York

APPENDIX B

SOME fifty-nine¹ countries have been granted monetary aid from the United States in the postwar period. Below, according to the compilation of Prentice-Hall, Inc., are the countries to which more than \$13,000,000,000 went:

(In Thousands of Dollars)

<i>Albania</i> : Through UNRRA	\$40,502.
<i>Argentina</i> : Cultural and technical aid, bank credits	297.
<i>Austria</i> : Supplies, bank credits, surplus property	63,000.
<i>Australia</i> : Lend-lease and fixed war installations	54,894.
<i>Belgium</i> : Loans, Lend-lease, surplus property	494,000.
<i>Bolivia</i> : Cultural and technical aid	245.
<i>Brazil</i> : Bank credits, cultural and technical aid	70,680.
<i>Burma</i> : Lend-lease	11,000.
<i>Canada</i> : Alaska highway	138,312.
<i>Chile</i> : Bank credits, cultural and technical aid	42,195.
<i>China</i> : Export-Import bank credits, surplus property, Lend-lease	1,482,793.
<i>Colombia</i> : Bank credits, cultural and technical aid	859.
<i>Costa Rica</i> : Inter-American highway, cultural and technical aid	1,540.
<i>Cuba</i> : Cultural and technical aid	190.
<i>Czechoslovakia</i> : Export-Import bank credits and surplus property	31,304.
<i>Denmark</i> : Export-Import bank credits and surplus property	40,000.
<i>Dominican Republic</i> : Cultural and technical aid	75.
<i>Ecuador</i> : Bank credits, cultural and technical aid	1,288.
<i>Egypt</i> : War installations	11,800.
<i>El Salvador</i> : Inter-American highway, cultural and technical aid	327.
<i>Ethiopia</i> : Export-Import bank credits and surplus property	4,000.
<i>Finland</i> : Export-Import bank credits and surplus property	92,500.
<i>France</i> : Export-Import bank credits and surplus property	1,950,000.
<i>Germany</i> : Supplies	400,000.
<i>Great Britain</i> : Loan, surplus property	4,400,000.
<i>Greece</i> : Economic assistance, UNRRA, Lend-lease, surplus property	790,000.
<i>Guatemala</i> : Inter-American highway, cultural and technical aid	627.
<i>Haiti</i> : Cultural and technical aid	86.

(In Thousands of Dollars)

<i>Honduras</i> : Inter-American highway, technical and cultural aid	\$ 418.
<i>Hungary</i> : Surplus property	15,000.
<i>Iceland</i> : Fixed war installations	65,000.
<i>India</i> : Surplus property	50,000.
<i>Italy</i> : Economic relief, Export-Import bank loans, special considerations	538,000.
<i>Iran</i> : Surplus property, Lend-lease	30,000.
<i>Iraq</i> : Educational aid	41.
<i>Japan</i> : Supplies	267,000.
<i>Korea</i> : Supplies, surplus property	62,000.
<i>Lebanon</i> : Educational aid	90.
<i>Liberia</i> : Civic improvements	20,200.
<i>Mexico</i> : Bank credits, cultural and technical aid	87,574.
<i>Netherlands</i> : Export-Import bank credits, Lend-lease, surplus property	377,384.
<i>New Zealand</i> : Surplus property, war installations	5,707.
<i>Nicaragua</i> : Inter-American highway, cultural and technical aid	2,430.
<i>Norway</i> : Export-Import bank credits, Lend-lease	56,500.
<i>Panama</i> : Inter-American highway, cultural and technical aid	47.
<i>Paraguay</i> : Cultural and technical aid	38.
<i>Peru</i> : Bank credits, cultural and technical aid, war installations	2,930.
<i>Philippines</i> : War claims	695,000.
<i>Poland</i> : Export-Import bank credits, surplus property	90,000.
<i>Portugal</i> : War facilities	(value undetermined)
<i>Saudi Arabia</i> : Export-Import bank credits, surplus property	12,000.
<i>Spain</i> : War installations	136.
<i>Soviet Union</i> : Lend-lease	250,000.
<i>Syria</i> : Educational aid	10.
<i>Turkey</i> : Economic and military aid, Export-Import bank credits	270,000.
<i>Uruguay</i> : Surplus property, cultural and technical aid	733.
<i>Venezuela</i> : Cultural and technical aid	144.
<i>Yemen</i> : Surplus property	1,000.
<i>Yugoslavia</i> : UNRRA aid	(value undetermined)

¹ Nations not receiving U.S. aid: Afghanistan, Bulgaria, Ireland, Luxembourg, Romania, Siam, Sweden, Switzerland, Union of South Africa.

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